A large, abstract graphic in the background consists of numerous white triangles and squares set against a dark gray background, creating a sense of depth and motion.

JANUARY / 1961

THE MANAGEMENT REVIEW

THE MONTH'S BEST IN BUSINESS READING . . .

DIGESTS / FEATURE ARTICLES / BOOK REVIEWS

Special Features:

Before You Switch to Foreign Suppliers

*Executive Compensation: Gearing the Program
to Today's Needs*

A Realistic Look at Organizational Loyalty

Delegation: Eight Managers Who Won't Let George Do It

AMERICAN MANAGEMENT ASSOCIATION

Using recent experience profitably . . .

AMA Midwinter Personnel Conference

February 20-22, 1961 • Palmer House • Chicago

This AMA Conference stresses new techniques of personnel management and explains how forward-looking companies are using them to improve existing personnel programs. Conference speakers—authorities in their fields—will emphasize such topics as:

- *motivating workers to greater productivity*
- *management development*
- *personnel's role in sales training*
- *selecting sound decision-makers*

A special session on *labor relations* will cover new trends in union organization drives . . . control of industrial relations in multiplant operations . . . techniques for strengthening collective bargaining teams.

Those interested in *compensation* will find a session devoted to an over-all organizational approach . . . compensating technical and scientific personnel.

Special Conference Feature: A strike panel led by Victor Riesel will explore before, during, and after aspects of three recent strikes. Executives of the companies involved will participate as panel members.

Other conference presentations will cover adjusting personnel programs to meet the challenges of the future, new concepts in appraisal, composition of tomorrow's work force, corporate responsibility in education, and managing in changing times and conditions.

Insure attendance at this important meeting by registering now. Write, wire, or phone AMA, 1515 Broadway, New York 36, N. Y.—Judson 6-8100.

AMERICAN MANAGEMENT ASSOCIATION, INC.



in this issue...



- **Back in Your Own Back Yard.** During the past two years, the number of companies shifting from domestic to foreign sources of supply has doubled and, in the great majority of cases, lower price was the only reason for making the changeover. In this month's opening article, IRVING LIPKOWITZ examines the effect this situation is having on foreign competition and the current balance-of-payments problem, and he points out the advantages—some of them more important than price alone—that companies can enjoy by purchasing from domestic suppliers.
- **Executive Compensation Today.** Expanding profit opportunities and sharper competition during the sixties will increase the need for high-caliber management talent—and financial compensation will continue to be the number-one factor that attracts, keeps, and motivates most executives. On page 9, RICHARD SMYTH discusses over-all trends in executive compensation and outlines today's requirements for a soundly balanced program.
- **What Kind of Loyalty?** In his article on page 19, NATHANIEL STEWART attempts to arrive at a clearer definition of organizational loyalty: what it is and is not, how it develops, what kind of loyalty management has a right to expect—and some of the unrealistic expectations that are occasionally cherished by top executives.
- **Delegation at Large.** Everyone talks about delegation—and some people do all the wrong things about it. For a glimpse at eight types of managers whose approach to delegation leaves more than a little to be desired, see this month's cartoon feature, which begins on page 15.

—THE EDITORS

JANUARY 1961
Volume ~~XXX~~, No. 1
50

THE MANAGEMENT REVIEW

FEATURES

- 4 Before You Switch to Foreign Suppliers
By Irving Lipkowitz
- 9 Executive Compensation: Gearing the Program to Today's Needs
By Richard Smyth
- 15 Delegation: Eight Managers Who Won't Let George Do It
Cartoon feature
- 19 A Realistic Look at Organizational Loyalty
By Nathaniel Stewart

BUSINESS DIGESTS OF THE MONTH

Trends and perspectives

- 25 The Economy in 1961: 327 Top Economists Look Ahead
(Architectural Record)
- 29 Fringe Benefits Around the World
(First National City Bank Monthly Letter)
- 41 New Standards for Consumption?
(Business Week)
- 50 Next, the Solid-State Vice President
(Fortune)

Management policy and practice

- 35 How Companies Are Using Product Managers
(*Printers' Ink*)
- 38 Seal of Approval: The Role of Independent Testing Laboratories (*Industrial Design*)
- 44 Employee Selection: How Valid Is Personnel Testing?
(*Industrial Relation News*)

Operating guides for executives

- 47 Scrap, Waste, and Spoilage: Dollars Down the Drain
(*The Price Waterhouse Review*)
- 53 What's Wrong with PR Overseas?
(*Charles E. Allen*)

What others are doing

- 32 Cutting the Costs of Small Shipments
(*The Wall Street Journal*)
- 56 Convenience—Newest Necessity in Packaging
(*Modern Packaging*)

D E P A R T M E N T S

Also Recommended—Page 59

Brief summaries of other timely articles

Survey of Books for Executives—page 85

Cover Photograph: Socony Mobil Oil Co., Inc.

HARWOOD F. MERRILL, *Editorial Director*

VIVIENNE MARQUIS, *Editor*

ROBERT F. GUDER, *Managing Editor*

PETER HAAS, *Digest Editor*

JULIET M. HALFORD
Book Review Editor

LYDIA STRONG
Contributing Editor

GRACE T. COMPTON, *Assistant Editor*

THE MANAGEMENT REVIEW is published monthly by the American Management Association, Inc., at 1 Sherman Avenue, Jersey City 7, N. J. Main offices at 1516 Broadway, Times Square, New York 36, N. Y. Form 3579 should be sent to 1516 Broadway, Times Square, New York 36, N. Y. Second class postage paid at Jersey City, N. J. Subscriptions: \$7.50 per year (nonmembers, \$12.50). Single copies: \$1.00 (nonmembers, \$1.25). Volume XLX, No. 1, January, 1961.

Changes of address should be forwarded to the publishers six weeks in advance, and postal zone numbers should be included in all addresses.

The American Management Association does not stand sponsor for views expressed by authors in articles issued in or as its publications.

An index to THE MANAGEMENT REVIEW is published annually with the December issue. The contents are also indexed in the Industrial Arts Index through December, 1957, and from January, 1958, in the Business Periodicals Index. THE MANAGEMENT REVIEW is microfilmed by University Microfilms, Ann Arbor, Mich.

Copyright © 1961 by American Management Association, Inc.

The dramatic increase in the number of companies shifting to overseas sources of supply has been caused primarily by the lure of lower prices—but there are other factors that should be weighed carefully . . .

Before You Switch

THE U.S. BALANCE-OF-PAYMENTS DEFICIT that has sprung into front-page prominence has suddenly focused national attention on foreign spending. The Administration has taken some steps toward correcting this deficit—and the resultant outflow of gold, which had reached the rate of \$3.8 billion a year in July and, by October, stood at an annual rate of \$5.9 billion—by cutting the federal government's overseas military spending and reducing the number of military dependents abroad. But the problem is not the government's alone—any foreign spending, by government or industry, contributes to the deficit in balance of payments. As long

■ ***Irving Lipkowitz***
*Director of Economic Affairs
Reynolds Metals Company*

To Foreign Suppliers

as the deficit persists, private industry must share the national responsibility of reducing overseas spending. And the fact that possible reductions in the government's military and economic aid expenditures are limited under today's international conditions throws a large part of the burden directly on the activities of private industry.

How does this affect an individual company's purchasing policies? It would be an unusual company that could afford to select its suppliers solely on the basis of the international balance-of-payments situation, of course, but the very existence of the substantial U.S. deficit might well cause many corporations, for the sake of enlight-

ened self-interest, to examine their purchases from overseas sources. When they do, a good many will find that they have been overlooking some of the not-entirely-obvious benefits of domestic purchasing for the sake of immediate—and sometimes illusory—price advantages overseas.

It's clear that most companies shift from domestic to foreign purchasing of raw materials or components because of the lower prices that prevail abroad. A recent *Purchasing* magazine survey indicated that fully 70 per cent of those who switch to foreign sources of supply do so solely because of price considerations. Only 22 per cent make the change because of quality considerations.

PRESSURE ON PRICES

At first glance, this would seem entirely appropriate, since it is usually taken for granted that a company should buy its raw materials and components where it can get them cheapest. Under today's business conditions, it would be particularly unrealistic to dismiss lightly the lure of foreign prices to the purchasing agents of domestic companies. A large and growing number of industries are finding that the domestic supply of the products they sell exceeds the domestic demand. In addition, imports are entering their markets, and they are becoming more and more involved in intense competition with other industries. All these conditions create such a powerful downward pressure on selling prices that the individual company is forced to seek ways and means of cutting costs. What better way to cut costs than by buying cheaper? And if that means buying foreign, why not do so?

Unfortunately, the cost-price squeeze is not solved that simply. If, as the modern purchasing agent properly claims, purchasing policy must be considered an integral and indivisible part of a company's total guiding policy, more than price statistics must be taken into account.

Basically, a company must buy, just as it manufactures and sells, where it does the company the most good. From that viewpoint, the purchasing agent must be as mindful as the salesman of the fact that every company's first need is a good market. A good purchasing policy must be cost-sensitive—but it must also be market-sensitive. If a particular purchasing policy jeopardizes the market in which

a company must sell most of its output, the soundness of that policy is open to very serious question.

With 96 per cent of domestic manufactured goods being sold right here in the United States, most companies are obviously finding their best market in this country. Purchasing policy therefore must be concerned with the ability of that United States market to absorb a company's product. And the hard new fact that has to be kept in mind, whether purchasing, production, or sales policy is under review, is that no branch of American industry can any longer take for granted the availability of domestic markets.

A CRITICAL CROSSROAD

There is still time to make sure that foreign purchasing does not turn out to be very expensive and shortsighted bargain-hunting. Last year, a survey showed that 72 per cent of the companies covered had not yet made a shift from domestic to foreign suppliers. There is, however, a strong trend toward foreign purchasing: Within a two-year period, the percentage of companies shifting from domestic to foreign sources of supplies doubled, from 14 per cent to 28 per cent of the companies surveyed.

This shift to foreign sources necessarily has an adverse effect on the purchasing power of domestic suppliers and their employees. If the abandonment of domestic sources of supply becomes widespread, the resultant decline in domestic purchasing power could be general enough to affect the U.S. market in which the bulk of industry's products is sold.

It is vitally important, therefore, that companies considering a shift from domestic to foreign suppliers examine the basis on which their decision will be made. Is such a switch the reaction to price-tag pressure, or is it a result of a thorough evaluation of where the best total value can be obtained?

Industries that have customarily and traditionally purchased their supplies domestically naturally take United States conditions and attitudes for granted and assume that foreign suppliers will match them in all respects. They are not always aware that domestic sources of supply provide purchasers with special benefits that are by-products of our geography, our size, our advanced living standards, and our business and merchandising traditions.

Domestic supply industries, as a matter of self-interest, concentrate on serving their best customers—those located here in the United States. The best customers of foreign suppliers are also those located inside their own countries. While exports are relatively more important to other nations than they are to the United States, Western Europe and Japan still sell three times as much within their domestic markets as they export. The foreign suppliers' *total* exports therefore constitute a minor market, and the United States is but one segment of that minor market.

Contrast this with the predominant place of domestic purchasers in the domestic suppliers' market. There is no doubt that foreign suppliers want the business of American customers, but there is also no doubt that the United States customer is not nearly as important to them as he is to United States suppliers.

In addition, domestic suppliers are geared to United States markets. They have necessarily adapted themselves to their customers' needs over the years. Foreign suppliers find it necessary to be organized for flexibility in world markets, and they frequently find it most profitable to move in and out of markets quickly. For that reason, many foreign suppliers sell through trading companies and agents and cannot provide the various sales services that a domestic supplier can make available.

ADDED VALUES

The importance of the added values that are not reflected in price statistics is indicated by a check list used by a leading manufacturer of industrial and consumer electrical products in its systematic appraisal of total value in making its purchasing decisions. Under the heading of "Technical Capabilities," this check list includes such items as these:

- Will supplier provide application engineering assistance?
- Will supplier provide installation and service engineering assistance?
- Will supplier provide analytical engineering that will help improve the efficiency of my basic processes?
- Will supplier help train my operators?
- Will supplier provide design assistance?

(Continued on page 63)



EXECUTIVE COMPENSATION:

*Gearing the Program
to Today's Needs*

■ **Richard C. Smyth**

Smyth & Murphy Associates, Inc.

AS WE MOVE into the second year of the decade that has been widely hailed as the "Soaring Sixties," the air will be full of evaluations and predictions of trends and prospects in the economy. It is, of course, important and valuable that new problems should be discussed, new opportunities foreseen, and new challenges set forth—but we must not lose sight of the fact that a high level of executive competence remains at the top of the list of corporate necessities. The men who constitute American management will be the ones who will solve the problems, seize the opportunities, and meet the challenges of the future, and the task of attracting, retaining, and motivating top-caliber executives will continue to be of vital concern to every American business.

For this reason, many companies are taking a new look at their executive-compensation programs to determine whether they are still adequate and realistic in the light of today's business environ-

ment. A review of this kind can be valuable for any company—and for some it is long overdue. In many organizations, the various elements of management compensation have evolved over the years with no conscious regard being given to the creation of a systematic and balanced whole or to corporate objectives and philosophies. In some cases, the bargaining power of a specific individual or group has resulted in compensation inequities within the company; in others, a chief executive with private means or extensive stock ownership has held his own compensation, and that of his subordinates, unrealistically low; in still others, a board of directors consisting mainly of corporate officers has established management compensation at an unreasonably high level.

More common, perhaps, are the management-compensation programs that simply have not kept pace with the changing organization structure of the company or with the inflationary increases of the past decade, and the "programs" that are not programs at all but merely collections of unrelated pay devices.

BASIC OBJECTIVES

As a result, many companies have found that an objective, systematic, over-all review of their management-compensation program is highly desirable to assure that the program is in line with compensation levels in other companies and with corporate policies and objectives, as determined by the board of directors.

The basic objectives of any sound and comprehensive management compensation program are fourfold:

1. To *attract* the desired caliber of managerial talent from other companies or from subordinate positions within the corporation.
2. To *retain* the desired caliber of managerial personnel in the employ of the corporation.
3. To *motivate* management personnel to a sustained high level of personal performance to achieve corporate profit and growth objectives.
4. To *provide* the maximum tax advantage to the executives involved and to the corporation, consistent with our tax laws.

An adequate, fair, and effective management-compensation program will consist of a series of properly designed and interrelated

elements, the combined effect of which will be to achieve these objectives. There are four chief forms of executive compensation:

- Salary
- Incentive or bonus awards
- Deferred compensation
- Stock options

In addition, of course, members of management usually participate in the pension and insurance programs provided for all employees.

EXECUTIVE SALARIES

In most companies, salary is the most important form of management compensation, but it has usually received the least systematic attention in the development of the over-all program. Obviously, salary is the base on which a sound management-compensation program rests. Not only is it ordinarily the largest single element of compensation, but other elements of the program—notably pensions, insurance, and bonus awards—usually bear a direct relationship to base salary. Thus, any inequities in the salary structure tend to compound and become magnified in practice.

In view of the importance of salaries, it is surprising to see that relatively few companies have developed meaningful salary ranges for their different management positions. Naturally, a salary program at the management and executive levels should not be rigid and mechanistic, but the establishment of equitable salary ranges provides valuable guidelines for board or top-management action in setting the salaries of specific individuals.

Salary ranges should be established for the various management positions without regard to personalities. The group of functional responsibilities that constitute each position has a definite current salary value that can be determined realistically and objectively, taking into consideration the three main determinants of executive salary value: company size, industrial classification, and the internal relationship of management positions to each other.

Determining Salary Values

At the top-management and corporate-officer levels, the most important determinant of salary values is company size. Generally speaking, large companies pay more than smaller companies for posi-

tions of equivalent functional content. An analysis of 82 durable-goods manufacturing companies, for example, shows a consistent increase in the salaries paid to the chief executive officer and other officers as corporate size increases.

The next consideration in determining salary values at the management levels is the specific industry involved. Considerable variance exists in the salaries of the same management positions in different industries, and salaries in any particular company will naturally reflect current practice in the industry of which it is a part.

The other significant determinant of executive salary values is the relationship of management positions to one another within the company itself. At the officer and manager levels, direct comparison with the salaries paid by other companies can be made for 30 to 50 per cent of the positions involved, but because of differences in organization structure and the varying functional content of different positions in different companies, it is not always possible to secure valid comparisons. In these cases, some basis of interpolation is needed to relate salaries within the company to those paid by other organizations. This can be done on the basis of job-to-job comparisons, or it can be determined on a factor-by-factor basis, using a simplified position-evaluation plan to determine relative position values.

At the management levels, salary ranges have a typical spread of about 50 per cent—that is, the maximum of the range is 50 per cent greater than the minimum. The median salary paid by other employers is ordinarily used as the midpoint.

When applied with due consideration for position differences, this concept results in meaningful salary guidelines for each management position in the company. The salary ranges are related to the relative significance of the positions within the company, the nature of the industry, and the size of the company, and they can be readily justified to stockholders, directors, individual executives, the internal revenue service, and the renegotiation board.

INCENTIVE OR BONUS PLANS

In general, the salaries paid management personnel tend to relate to company size, while additional compensation tends to relate to company profitability.

One major element of additional compensation is bonus or incentive awards. About half of the larger companies in the country already have incentive bonus plans, and the trend seems to be toward their increasing use.

The basic concept underlying such plans is that a portion of the earnings of the company should be shared with the management group that created the profits, in order to motivate management to create more and larger profits in the future. Generally, a portion of earnings is first set aside as a basic return for capital employed in the business, and a percentage of the balance is then used to create a bonus fund from which awards are made to management personnel.

Bonus Fund Formulas

Under some plans there is no specific formula, and the amount to be set aside for management bonuses is determined each year on an *ad hoc* basis by the company's board of directors after the books are closed and audited. There is, however, a growing use of predetermined formulas for the creation of bonus funds. For example, the basic bonus plan formula of the General Motors Corporation is "12 per cent of the net earnings, after deducting 5 per cent on net capital." The Ford Motor Company's formula is essentially "6 per cent of the company's net income before taxes, but after deducting 10 per cent on total capital investment."

Surveys indicate that more than two-thirds of all incentive bonus plans currently use a predetermined formula, on the theory that this provides a far more powerful incentive to the executives who will participate in the plan, since most people will put forth more effort to secure a known reward than a reward of an unknown nature or amount.

Obviously, the bonus-fund formula can be based on profits before or after taxes. It can be argued that before-tax profits are a better measure of the results achieved by management, since management has no control over corporate taxes and merely pays the amount that is legally required. Moreover, a formula based on corporate pre-tax earnings does not have to be modified to prevent windfalls to executives as changes take place in the corporate income tax rates. On the other hand, a formula on an after-tax basis has the

major psychological advantage of placing the company's executives on the same basis as everyone else in the minds of the stockholders.

Regardless of the formula used, two major questions must be answered: "Who shall participate in the incentive bonus plan?" and "How shall the bonus fund be distributed?"

Participants

The number of participants in the bonus plan will depend on the business philosophy underlying the use of the plan and the anticipated size of the individual bonuses. In some companies, a bonus is used to augment otherwise low salaries, and that part of the salary paid as bonus is a variable item relating to corporate profitability instead of being a constant item of overhead. In other companies, the bonus is a reflection of an attitude of paternalism and becomes, in reality, a gratuity or "Christmas present." This is typical of many European companies, where a thirteenth month's salary is given at the end of the year. Where these concepts prevail, bonuses are usually rather small and extend far down into the organizational structure.

A different and more positive management concept is to establish a fair, equitable, and competitive salary structure and then to build an incentive bonus plan on top of this structure. Under this concept, the purpose of the bonus is to motivate management to a level of personal and group performance that will achieve a high return on invested capital, and participation is limited to those members of management who make or significantly influence *profit decisions*. Accordingly, the number of participants tends to be small, and the individual bonuses tend to be large, making the managerial outlook and rewards more nearly those of the entrepreneur.

In most companies, the higher-level line positions *make* decisions that affect profits, and the higher-level staff positions *influence* these profit-making decisions. These are the managerial positions that logically should be included in an incentive bonus plan. Any incentive or bonus plans covering lower-level line and staff positions usually should not be based on the profit-and-loss statement, since positions at this level do not have a significant or measurable effect on the corporate picture.

(Continued on page 70)

DELEGATION: 8 Managers Who Won't Let George Do It

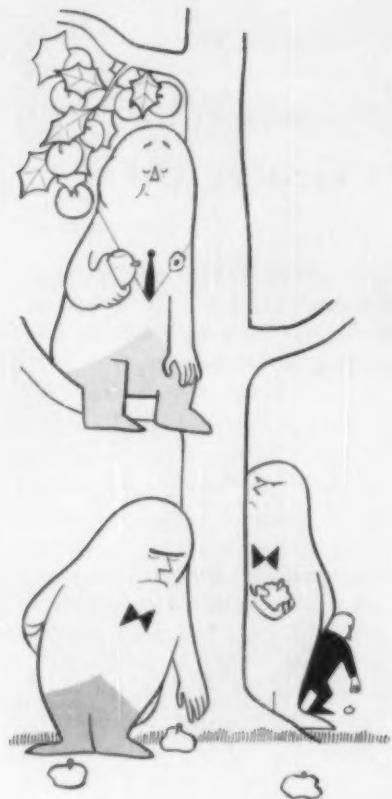
BY DEFINITION, management involves getting things done through others—and this means that the problem of delegation will always be with us. Here are eight types of executives whose approach to this problem leaves something, if not everything, to be desired . . .



Indian Giver. Maybe he should have assigned that job to someone else. Maybe he should be doing it himself. Maybe it shouldn't be done at all. Better take it back until the whole matter can be reconsidered.

Pinkerton. He's delegated the job, but it's still his responsibility, and by George he's going to see to it that every *i* is dotted and every *t* crossed. After all, he's the boss—and everyone appreciates guidance.



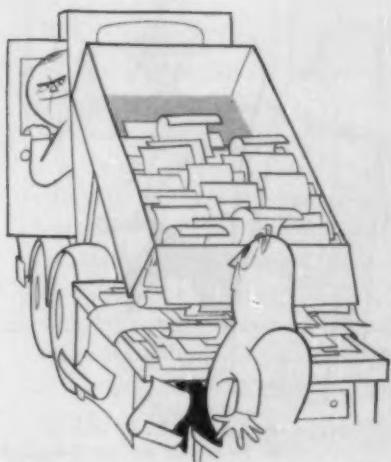


Plum Gatherer. He's perfectly willing to delegate—but only the disagreeable parts of the job.

Miser. No use burdening one man with the entire job; it's kinder to split everything up among several people. No one will ever get a clear picture of what's involved, but at least it spreads out the work.



Time Bomb. All right, so he'll delegate—but woe betide any subordinate who is luckless enough to make a mistake.

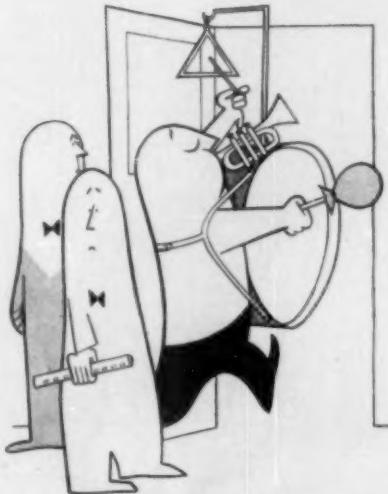


Dumper. Delegation—what a glorious excuse for unloading the whole job and leaving himself free for a round of golf of an afternoon! His subordinate may not be prepared for the added responsibility, but what better way to test a man's mettle?



Star Performer. He's the one who handed out the jobs and masterminded the whole shooting match, so why shouldn't he take all the credit?

One Man Band. Long experience has taught him that the only way to get a job done right—that is, the way *he* would have done it—is to do it himself. There's plenty of clerical work to keep the others occupied—and they never seem to stay with the department very long, anyway.



■ *Text by R. F. GUDER*
■ *Drawings by AL HORMEL*



A REALISTIC LOOK AT

Organizational Loyalty

■ *Nathaniel Stewart*

*Director, Management Development Center
International Cooperation Administration*

WITH THE PROFIT SQUEEZE becoming tighter because of rising costs of labor, materials, services, and other requirements, it's a fortunate company that can count on the loyalty of its people—not only in the ordinary, everyday activities on the job, but also in the critical and extraordinary situations in company life. It can be tapped by more companies, for we are now reaping the rewards of psychological research and have come to understand that employee loyalty is a phenomenon that is highly individualized, yet also an outgrowth of the dynamics of a cohesive work group. Organization-centered loyalty must be harnessed from both sources. It cannot be demanded, manufactured, procured, or gimmicked—it has to be earned.

One reason many companies fail to get the loyalty they are seeking

lies in their misconceived and unrealistic ideas of just what loyalty is. From the exhortations emanating from some executive suites, one might well conclude that what the company is looking for is blind, unquestioning obedience and fidelity, with never a voice raised in protest or disagreement. Actually, of course, blind loyalty of this kind should not be expected by management, nor should it be in any way encouraged. Even if this kind of uncritical commitment to the company should be attained, at best this employee reaction is shallow, transient, and lacking in conviction.

Too often, management tends to judge employees' reactions to certain situations in terms of loyalty, even though the question at hand has nothing to do with it. If a man feels, for example, that he has been unfairly treated and raises what he considers a legitimate grievance; if he is less than enthusiastic about accepting a situation that seems to him unreasonable; if he questions the wisdom of a course of action that has been prescribed by higher management—in such instances as these, the man is not being disloyal to the company. He may be acting in the light of his own principles and beliefs, or those of the informal group he represents—and he may be right. At any rate, he is certainly a more valuable member of the company than the ambitious individual who will go along, chameleon-like, with almost any change or decision because it seems to be expedient at the moment to do so.

WHAT MANAGEMENT CAN EXPECT

Does this mean, then, that a company should not expect loyalty from its executives and employees? Not at all. It does mean, however, that top management must have a clear idea of just what kind of loyalty it has a right to expect. Basically, the company can expect every employee to manifest loyalty in six areas of everyday company activities:

- He should render a fair day's effort and work, both in output and quality, for the salary he receives.
- He should contribute to and foster a friendly and harmonious work relationship with his associates and others in the company.
- He should respect and carry out company rules and the orders of his superiors.

- He should accept constructive criticism and seek to improve his subsequent performance.
- He should speak well of the company in his relationships with customers, suppliers, and others in the business world and in the community.
- He should respect the organizational structure and stay within channels in having his work reviewed or in communicating a need, a proposal, or a grievance.

In addition to these ordinary requirements, the company can also expect its employees to exhibit their loyalty in unusual or critical situations: When, for example, the going is tough and there is to be a tightening of the belt; when more work and responsibilities must be assumed—for the time being, at no additional compensation; when there is the urgency of a serious cost-cutting program; when productivity standards must be raised; or when the company plans to install a change in the organization that has some impact on the employee's work conditions, skills, work habits, or social relationships on the job.

WHAT IS LOYALTY?

All these are, of course, manifestations of organizational loyalty, not definitions of it. Loyalty to a company is an elusive concept that isn't easily identified. Management may be too idealistic when it expects all employees to be "loyal" to the company's over-all objectives and to the philosophy of the free-enterprise system. Such things are simply too distant from the goals and values of employees at lower levels of the organization to be very meaningful, although they may acknowledge them in principle or recognize their importance in the economics of the industry. They become more important to men at higher levels of management—where, fortunately, loyalty to such fundamentals is more necessary to the company.

Organization-centered loyalty can probably be defined as a man's strong personal commitment to give more than adequately of his time, energy, talents, judgment, ideas, and moral courage in the best interests of the company with which he is affiliated. Within this personal commitment—both in giving more than adequately and in giving his best efforts when the company is in a pinch—there is an element of self-centeredness. That is, as a free agent he places a

certain value on his own time, talents, aspirations, special abilities, and energy. He weighs these, as well as his potential contribution, against the value that the *company* places on them. And the only tangible way in which he can assess this value is in terms of (1) the management creed, or beliefs that the company proclaims it stands for, and (2) the actual work environment that the company provides — how well it utilizes his abilities and provides fair salaries, stability of employment, opportunities for advancement and promotion based on judicious appraisal, respect for the informal as well as the formal organization in the development of standards, up-to-date facilities or tools to enable a man to work well, and opportunity to have some voice in participating in decisions or matters that affect him or his productiveness.

If management places a merited value on these factors more or less comparable to the value which the man places on them, his loyalty to the company is enlarged. If it is indifferent to or places a low value on these, the man's loyalty will be only marginal or limited. The more both the company and the man see eye to eye on the assessment of values, the more the various components of loyalty will build into organization-centered loyalty. The main question is not whether employees are generally loyal to the company but the *degree* of loyalty.

COMPONENTS OF LOYALTY

Practically speaking, organizational loyalty is a composite of several kinds and dimensions of loyalty that are present to some degree in all employees.

Loyalty to Occupation

The first is one's loyalty to his profession, occupation, or craft. This kind of loyalty is most obvious in the man we recognize as a dedicated newspaperman, engineer, chemist, or other professional, but it is present to some extent in all occupations. Occupational loyalty derives from a man's pride in the craft for which he was trained and which he practices, and from his continuing affiliation with others similarly trained—in some cases, through membership in a professional society or trade association.

Each member of the organization will observe how well the company's performance measures up to the generally accepted standards

in his own field, and his loyalty to the company will be increased or diminished accordingly.

Loyalty to the Work Group

Another element is loyalty to the work group—to fellow workers or close associates in the company. This aspect of loyalty bears significantly on morale and productiveness. Psychological studies of high- and low-producing groups of workers indicate that immediate work-group loyalty, a derivative of the informal organization or clique, is a more significant factor in cohesiveness, morale, and productivity than is general loyalty to the organization as a whole. Studies of group cohesiveness or work-group loyalties in banks, public utility companies, insurance firms, and other enterprises have repeatedly confirmed this loyalty element and its impact on clerical employees, engineers, assembly-line workers, and others.

Loyalty to Superiors

Allegiance to one's supervisor is another dimension of loyalty in modern business and industrial enterprise. When the supervisor demonstrates his interest in the men and their problems by training his subordinates, displaying fairness in allocating rewards and recommending people for merit increases or promotions, and going to bat for his men on key issues, the result is usually the formation of strong bonds of personal loyalty. This kind of loyalty, valuable throughout the organization, is perhaps most important at the first- or second-line supervisory level, for it is here that the employees find out whether management means what it says, practices what it preaches, and translates company personnel policies into meaningful actions.

Loyalty to the Product

Pride in the products or services in which the company deals is another aspect of loyalty. It is demonstrated in the salesman's enthusiasm for what he is selling, the engineer's determination to design the best possible model, the production worker's application of extra care and craftsmanship at his work station. Loyalty to the company's product is found in all branches of business and industry, whether it be the manufacture of toys, the proofreading of manuscripts in a

publishing house, or the production and marketing of household chemicals.

Institutional Loyalty

Closely allied to product loyalty is what we might call institutional loyalty—the pride of an employee in the prestige and reputation that his company has earned over the years. Employees and executives are often willing to sacrifice other advantages (in the form of wages and salaries, fringe benefits, etc.) in order to work for a company in which they can take justifiable pride.

MOTIVATION AND MORALE

For the most part, the forces that influence employee loyalty are internal. Only to a limited extent is it influenced by external forces such as technology, changing cultural values, social movements, political changes, or even general economic trends.

The internal forces that strongly affect employee loyalty are these:

- The motivational influences that act upon the individual in his work situations.
- The impact of company climate on group morale in the informal organization.

Obviously, these two vital considerations are affected to a considerable extent by the company's personnel policies and the caliber of supervision.

Motivation and Loyalty

The literature of human relations and personnel psychology treats motivation extensively—and defines it in various ways. It has been expressed as the combination of needs: the need to belong, the need for security, the need to get ahead, the need for freedom of action, the need for challenge, and need for recognition. Similarly, psychologists at the Survey Research Center of the University of Michigan list the basic components of motivation as the need for recognition, achievement, autonomy, affiliation, security, and evaluation.

An articulate listing of motivational factors was compiled by John Troxell of Stanford University's Graduate School of Business as the basis for an attitude survey.

(Continued on page 80)

BUSINESS DIGESTS OF THE MONTH

The Economy in 1961:

327 TOP ECONOMISTS LOOK AHEAD

By Edwin W. McGee, Jr.
and Edward A. Sprague

*Condensed from
Architectural Record*



BUSINESS ACTIVITY is expected to dip mildly during the next six to nine months but will start moving upward again by late 1961. So say approximately two-thirds of 327 leading economists polled by the F. W. Dodge Corporation in its latest annual survey. Although the consensus points to some degree of recession in the coming year, several strengths in the economy should keep the dip relatively mild and fairly brief. Among them:

- Business managements have already noted the slow-up in sales, and many adjustments are already behind us.
- The impending downturn in plant and equipment comes when our economy is less heavily weighted by manufacturing than by nonmanufacturing (especially service) activities.

Architectural Record (November, 1960), © 1960 by F. W. Dodge Corporation.

- The economy has successfully weathered a fairly sharp economic change from a federal deficit to a modest surplus.
- Business psychology, which tends to swing violently, may well be too cautious about 1961 prospects.
- Sharp economic setbacks invariably follow periods of unsustainable activity; there are few such obvious excesses now, so there should be no deep slide in 1961.
- A new administration will have some "new" ideas.

Here are the economists' specific forecasts for ten major economic indicators:

1. Gross National Product

The median expectation of the economists is that the Gross National Product will inch gently upward from \$505 billion in the second quarter of 1960 to \$507 billion in the second quarter of 1961, and then move ahead more sharply to \$515 billion in the final quarter of this year, but this median estimate does not seem to reflect the general consensus of the economists. The 50 per cent range (that is, the 25 per cent of the replies on each side of the median) is quite wide for the second quarter of 1961, ranging from \$498 billion to \$512 billion. This spread continues through the end of 1961, with the total range extending considerably further downward than upward, indicating somewhat less optimism than shown by the median.

According to a special analysis of the individual forecasts, fully two-thirds of the economists expect to see some downturn in the GNP during the year, while only 30 per cent

of them anticipate a steady uptrend.

Most of the economists expect the GNP to reach a low point and to turn up again sometime before the end of 1961.

2. Industrial Production

The expected dip in economic activity in the months ahead is more clearly reflected in the economists' forecasts of industrial production as measured by the Federal Reserve Board index. On a seasonally adjusted basis, the index stood at 109 in June, 1960 (1957=100). The median expectation is that production will drop to 107 by June, 1961, after which it will rise moderately to 110 by the end of the year. However, the 50 per cent range runs from 102 to 111. This spread is maintained through the last half of the year as well.

Industrial production is forecast to dip more perceptibly than GNP, chiefly because of two factors. First, the index of industrial production is in terms of physical volume, while GNP is measured in dollars. More important, most of the economists feel that manufacturing industries will bear the brunt of the recession, reflecting plant and equipment cutbacks and inventory corrections.

Special analysis indicates that the expected pattern of movement is akin to that of the GNP. For example, nearly one-quarter of the respondents feel that industrial production will move steadily upward in the year ahead. A small number (3 per cent) expect a steady downward trend, another 10 per cent expect rising production in the near future but a declining trend by the end of 1961,

while the majority foresee a downturn at some time during the forecast period, followed by recovery shortly afterward.

3. Consumer Prices

Continued rise in consumer prices is expected by most of the economists. The consensus, however, is that the rise through 1961 will be no more than a "creep," with the median forecast of the consumer price index at 128.0 in December 1961—barely 1 per cent above mid-1960. The 50 per cent range of forecasts runs only from 127.0 to 128.7 for December, 1961, and there was a decided preference for 128.0 as the mode.

Despite the popularity of the 127-129 range, 11 per cent of the economists think the December, 1961, index will be lower than the 126.5 figure reported for June, 1960. This proportion of price "bears" is considerably higher than found in the surveys for 1959 and 1960.

Quite a few economists remarked that a mild recession in 1961 would act to weaken, if not halt, the upward price movement. Still, the undercurrent of feeling was that the long postwar inflation would continue and reassert itself, particularly in the second half of next year. Price increases are expected to be concentrated in the food and services sectors.

4. Wholesale Prices

Wholesale prices will inch up in 1961, but by less than the increase in consumer prices, according to a majority of economists polled. Both the median and modal estimates of the wholesale price index for Decem-

ber, 1961 are 120.0, as compared to the June, 1960, mark of 119.5. Again, the 50 per cent range is small, extending only from 119.4 to 120.7 at the end of next year.

Many of the economists expect some decline in wholesale prices. Twenty-four per cent of them set the December, 1961, index lower than mid-1960. Scattered among the replies were many comments to the effect that easing demand, oversupply of some materials, and competitive conditions will tend to keep a lid on wholesale prices in 1961. Cited among the factors exerting upward pressure was "cost-push" and the likelihood that the recent firming in food prices would strengthen in 1961.

5. Total New Construction

Total new construction, while down slightly in the second half of 1960, is expected to rise slowly to a seasonally adjusted annual rate of \$56.0 billion for the second half of 1961. The 50 per cent range extends further downward than upward, particularly for the first half of 1961, when several economists expect the annual rate to be below \$50 billion, but only two set it higher than \$59 billion.

In general, the points of strength this year will be residential building and public works, while nonresidential building will slacken.

6. New Housing Starts

Private nonfarm housing starts averaged 1,275,000 on a seasonally adjusted annual rate basis during the first half of 1960. The economists' median forecasts are for an annual rate of 1,300,000 in the first half of

1961 and 1,350,000 in the second half of 1961. As with the new construction estimates, the 50 per cent range reaches further downward than upward in both halves of 1961. There is a definite modal preference for 1,400,000 in the second half of 1961 but with a long, thin trail of forecasts from 1,250,000 on down comprising the lowest quartile.

7. New Plant and Equipment

New plant and equipment expenditures will decline in 1961, according to a great majority of the economists polled. The median forecasts for both halves of 1961 are \$35.0 billion (seasonally adjusted annual rate), which would represent a 5 per cent decrease from the estimated \$36.9 billion rate for the second half of 1960. Actually, most of the economists expect a divergent pattern for the two halves of the year, but the forecasts of an early dip tend to offset those that foresee a weaker second half. The whole range of forecasts is thus very wide. For the second half of 1961, 18 economists anticipate plant and equipment expenditures to run at \$30 billion or under, while 16 put the rate at \$39 billion or more.

8. Average Hourly Wages

The economists were asked to indicate whether 1961's average hourly wage trend would be up, down, or unchanged in the categories of durable goods manufacturing, nondurable goods manufacturing, and building construction. One economist, after checking the three "up" blanks in his survey form, summed up the feeling of a healthy majority with the simple question: "Where else?" Not more

than 2 per cent of the respondents thought wage rates would be down in any of the three categories.

Quite a few economists, however, predicted that wage increases would be modest this year, that a mild recession would dampen the long-term rise. About 19 per cent of the economists expect stability in durable goods wages; 15 per cent in nondurable goods; and 20 per cent anticipated no change in building construction wages.

9. Personal Consumption

Personal consumption expenditures will climb to a new high in 1961, recession or no recession, say most of the economists. The median forecasts are that consumer expenditures at seasonally adjusted annual rates will move to \$332 billion in the first half of 1961 and reach \$336 billion in the second half. Nevertheless, the mild downturn anticipated in GNP and industrial production is reflected to some extent in the forecasts of this series. The 50 per cent range for the first half of this year extends downward to \$327 billion, slightly below the current rate, and upward to only \$335 billion. For the second half of 1961, the 50 per cent range runs from \$330 billion to \$342 billion, with a fairly pronounced modal preference for \$340 billion.

10. Money and Interest Rates

An overwhelming majority of the economists look for relative stability in interest rates through 1961. The median estimates for June, 1961, are pegged at 3.2 per cent, with a slight rise to 3.4 per cent indicated for December, 1961. ♦

FRINGE BENEFITS around the world

Condensed from

The First National City Bank Monthly Letter

IN THE PAST 25 YEARS, fringe benefits have mounted to where, today, they commonly add 20 or 30 per cent to the U.S. wage bill—a matter of concern to businessmen who consider fringes a handicap to American industries competing with foreign manufacturers.

Now similar developments are causing concern abroad. Many countries overseas have created an even greater diversity of nonwage benefits than exists in this country. These benefits—as U.S. firms setting up branches abroad have discovered—can often run total employment costs far above the expense of basic wages. In many cases, firms contemplating overseas expansion have had to make special studies of benefits before they could calculate and compare true labor costs.

In Italy, for example, fringe benefits—called "social charges" in Europe—add on nearly 75 per cent to wage costs, according to a recent survey by the French National Institute of Statistics and Economic Studies. Italian employers pay for these charges through employment taxes.

In France, employers contribute more than 50 per cent in social charges beyond regular hourly wages,

while German firms are paying an average of about 44 per cent in fringe benefits. Costs of fringes vary not only from country to country but from one industry to another. In the Italian chemical industry, fringes are now almost as large as the regular wage, compared with an average of 25 per cent of wages in the U.S. chemical industry.

In Canada, fringe costs are also climbing and now average about 16 per cent of payroll, according to a private survey. In Latin America, supplementary benefits are also an important part of employment costs, although—as in many other parts of the world—they are difficult to measure. For example, the effect of providing high rates of severance pay cannot be readily calculated in dollars and cents.

Paying for Social Security

The big difference in fringe costs to employers around the world is where the main burden of social security financing is placed. In Italy and France, where social charges are relatively high, most of the social insurance bill is paid by employers through payroll taxes. In the United Kingdom, which has an extensive

First National City Bank Monthly Letter (December, 1960), The First National City Bank of New York.

cradle-to-grave welfare system, the employer's payroll tax amounts to only 3.3 per cent of the worker's wage; contributions from workers and the self-employed, together with general tax revenues, pay most of the bill.

Swedish employers, who previously paid only 1.1 per cent of wages for social insurance, had an additional 1.9 per cent tacked on in 1960 with the adoption of a new retirement scheme to supplement the existing pension system. In Denmark, business firms contribute nothing directly in support of their old-age pension schemes, but in Norway the employer's share is fixed at 60 per cent of a worker's contribution. A similar contrast is found in Australia and New Zealand. Though both countries have had welfare-minded governments, the costs of social insurance are shared differently. Business firms in New Zealand must pay 7½ per cent of their net income for social security; Australia's welfare scheme is paid for entirely out of general tax revenues.

Family Allowances

One type of benefit not found in the United States—family allowances—weighs especially heavily on employers in a number of countries overseas, particularly France and Italy. France's system of maternity and family allowances requires business firms to pay as much as 14½ per cent of payroll into a government fund. These allowances are paid out as wage supplements so that a worker with two children, for example, gets 22 per cent more than his basic wage, a worker with three children 55 per cent more. In Italy, the employer's contribution to the family allowance

system may run as high as 33 per cent of the worker's wage. Family allowances in the United Kingdom, on the other hand, are paid for out of general tax revenues, and business firms are spared from making direct contributions.

Higher and Higher

Though social security costs are the basic fringe items paid for by employers in most industrial countries, many business firms offer additional benefits of various kinds. These often include housing subsidies, health and recreation schemes, training grants, disability pay, free or subsidized meals, and special bonuses. In Italy, Christmas bonuses are usually fixed at the equivalent of 200 hours of regular pay. Collective agreements in some Belgian industries provide for profit-sharing by the workers.

In Japan, fringe benefits other than social security are largely the outgrowth of traditional practices. A worker is typically regarded as joining a company for life and usually stays on the payroll in good times and bad. This in itself constitutes a fringe benefit incalculable in money terms. Wages are based on the worker's age, education, length of service, and size of family. Because of chaotic living conditions and inflation after the war, twice-yearly bonuses and food and housing subsidies became firmly embedded in the wage system as a way of providing for a minimum standard of living.

In many other countries, paternalistic measures once regarded as odious by labor leaders have survived to be counted as fringe benefits today. Free or subsidized housing is often pro-

vided by employers in such countries as France, Germany, and Austria, according to a study published last year by the International Labor Office. Workers in Turkey commonly receive part of their pay in the form of food. Free coal for miners is a traditional kind of nonwage benefit still given in most countries, including the nationalized mines of the United Kingdom.

Payment for time not worked is another common type of fringe benefit, but one that is hard to measure. Legal holidays, paid vacations, sick leave, coffee or tea breaks, wash-up time, and similar periods of paid leisure vary considerably from country to country. In the Common Market countries, payment for days not worked ranges from 7 per cent of gross wages in Germany to 14 per cent in Italy, according to the magazine *Euromarket*. A large number of public holidays gives Italian workers more paid leisure than is enjoyed by most other Continental workers.

Competition in Fringes

Prosperity and the shortage of skilled workers are encouraging many business firms in Europe to offer more extra benefits as they bid for qualified help. The competition in fringes is especially strong in Germany and France, where labor markets are tight. But even in Japan, where labor is abundant, a shortage of engineers and scientists has caused some firms to offer study trips abroad and other advantages. In Germany, the fringe package currently offered by some employers includes generous pensions, profit-sharing plans, and plant-sponsored family trips.

In France, however, private em-

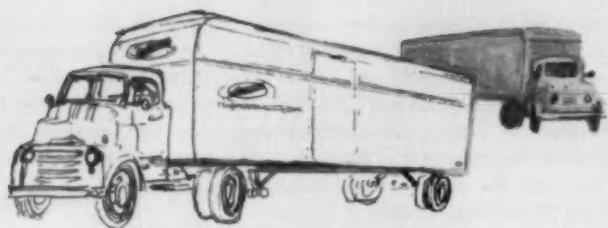
ployers must compete against the generous fringe benefits given by state enterprises, which employ about one out of every five industrial workers in that country. And these benefits are already hard to bear.

The Generous State

In his book, *The French Economy and the State*, Warren C. Baum lists the benefits given workers of the state-owned electric power company, *Elec-tricité de France*:

" . . . one month's paid vacation each year; two months' wages in case of marriage; full wages while on military service for fathers and 20 per cent of wages for bachelors; up to three years of full wages in case of illness; and one month's wages for the first child, one and one-half months' for the second and third, and two months' for the fourth. The age of retirement was set at 55 years for active workers and 60 years for sedentary workers, with the result that pension payments are among the highest in France. Employees also receive special benefits in the form of electricity, gas, coke, and coal provided free or at reduced rates. A fund for social activities of the employees has been established and is generously endowed by a 1 per cent levy on gross sales."

In general, career employees of government—sometimes relatively underpaid in the salary envelope—tend to enjoy the most generous fringe benefits. In addition, among industrialized countries, fringes are likely to be larger where wages are lower. Thus the differentials that appear in international comparisons of wages are likely to be moderated when fringe costs are added on. ♦



Cutting the Costs of *Small Shipments*

By Richard F. Janssen

Condensed from *The Wall Street Journal*

RECENTLY, Ekco Products Co. drove a truck trailer loaded with its products from its Ohio factory to Chicago. There, the company placed the trailer plus another one from its Chicago plant onto a piggyback railroad car bound for Minneapolis. The combined load made the trip for about \$237—about \$1,000 less than Ekco had been spending each week to make separate daily small truck shipments from the two plants to Minneapolis.

Consolidating many small shipments into a few big ones is only one of the steps Ekco and other companies are taking to cope with an increasingly severe problem: The skyrocketing cost and deteriorating service on small shipments.

The problem is particularly acute right now. The railroads have requested permission from the Interstate Commerce Commission to boost the minimum charges for small shipments

from \$3 to \$4 throughout the nation. Since last summer, five motor carrier rate-making groups have placed 10 per cent surcharges on small shipments, and others have asked the I.C.C. to authorize similar boosts. By one traffic authority's count, railroad and truck minimum charges for individual shipments have soared 512 per cent since 1946.

These boosts come at a bad time. Worried by possible recession, businessmen are trying to keep inventories as low as possible. So they are ordering more often and in smaller amounts. And while rates are climbing, service is slipping, traffic men say. "We get a carload shipment to Chicago from Seattle in seven days, but a less-than-carload order takes 12 days," grumbles a Chicago retailer. Increasingly, shippers say they can't even persuade a truck line to pick up a shipment destined for a customer

The Wall Street Journal (October 4, 1960), © 1960 by Dow Jones & Company, Inc.

in an out-of-the-way small community.

Efforts to solve the problem center on reducing the number of small shipments and combining them into big ones that travel at much lower rates per pound. There are a variety of methods open to cost-conscious shippers. Sizable savings can be obtained merely by consolidating shipments within a single company. "We save about \$35,000 a year by combining shipments from factories around St. Paul to our warehouse in St. Louis," reports F. L. O'Neill, general traffic manager of Minnesota Mining & Manufacturing Co. Plants at Hutchinson, Minn., and two other sites, for instance, route shipments first to the big St. Paul plant, where they are combined into trucks bound for St. Louis. The Hutchinson plant paid \$3.15 per 100 pounds when it sent less-than-truckload shipments directly to St. Louis, Mr. O'Neill says; now the plant enjoys a truckload rate of 19 cents per 100 pounds to St. Paul and 90 cents to St. Louis.

Internal Coordination

This sort of arrangement requires careful intracompany coordination, and it can even mean sharp changes in operating policy. For example, 2,400 retail stores in the Butler Bros. division of City Products Corp. each formerly sent in orders at will to the Chicago home office. "Now we're trying to eliminate small shipments," says Douglas R. MacDonald, general traffic manager. "Each store orders only on an assigned day of the week, and we can often send a store one 500-pound order a week instead of 50 orders of 10 pounds each." Rates, even on less-than-truckload shipments,

become progressively lower per pound as the weight of the shipment mounts.

Cooperating with Competitors

The urge to save money on small shipments is so strong that several well-known companies are now co-operating with their competitors. Every morning a big truck rolls through three New Jersey towns and stops at plants of Sterling Drug, Inc., Bristol-Myers Co., and the Whitehall Division of American Home Products Corp. "Instead of each company sending one-third of a truckload to New England every day, we now combine our shipments into one and prorate the savings from the truckload rate," relates Clarence D. Smith, traffic director of American Home Products. Annual savings to his firm: \$30,000.

Many companies achieve large savings by working out new shipping arrangements with their suppliers. Montgomery Ward & Co. is a leader in this direction, with its own formal freight forwarding system called Wardex. "Our savings with Wardex run in the millions of dollars every year," says Thomas Hope, Ward's general traffic manager. Mr. Hope figures Wardex moves freight at about 75 per cent of regular rates.

How does Wardex work? "Take a toy manufacturer in Kokomo, Ind.," Mr. Hope says. "He gets orders from perhaps all nine of Ward's mail order houses and hundreds of our retail stores. But instead of shipping to each store directly in small amounts, he will combine the orders into carloads and move them to our Chicago assembly point." Then Ward's will re-assemble the orders and move them to other "break points" such as Kan-

sas City, shipping full carloads or truckloads for as great a distance as possible and keeping the small-shipment segment to a minimum.

Using Warehouses

Ward's uses still another money-saving program. The company rents public warehouse space in Chattanooga, Tenn., and instructs northern manufacturers of refrigerators, freezers, ranges, and other heavy home appliances sold through its southeastern stores to send carload quantities to this warehouse. A store in Florida, for instance, orders appliances directly from the Chattanooga warehouse. The warehouse crew loads a full car with various appliances for the Florida store, and the store—taking advantage of "storage in transit" rates—pays the freight on each appliance as though it were receiving a full carload from the original source. Before the warehouse was set up, the stores had to pay higher rates for each appliance all the way from the manufacturer because none did enough volume to order a full carload of any one type of appliance.

International Harvester Co. of Chicago is another firm paying close attention to its suppliers' deliveries. Chicago-area suppliers of fuel pumps, generators, gaskets, and other farm implement parts route everything to a central point in the Windy City, where full truckloads are prepared for assembly plants in such places as Fort Wayne, Ind., and Louisville, Ky.

Simoniz Co. finds that the steep rates on small shipments make it worthwhile to increase sharply the number of its warehouses. "We have to stick to small shipments because

we have thousands of customers who can't accept more than a few cases at one time," says William Henderson, traffic manager of the Chicago-based auto polish firm. "Now we're using warehouses in 30 cities—10 more than a year ago," he says. It costs \$1.40 a hundred pounds to send a less-than-truckload shipment direct to a Detroit customer, he explains; the new way costs 50 cents per 100 pounds in a rail carload to a Detroit warehouse, 40 cents for warehousing, and 30 cents for local delivery—still a saving of 20 cents per hundred pounds.

Help from Piggybacking

Keeping abreast of newer methods of transportation is increasingly important, traffic men say. In some cases, piggybacking of a truck trailer on a railroad flatcar provides savings. Butler Bros. loads trailers with merchandise at its Kansas City warehouse for its St. Louis stores, and the van makes the rounds on arrival. The rate: \$1.30 per 100 pounds, a saving of 75 cents per 100 pounds compared to straight truck or rail rates. "Containerization" is attracting increasing attention, too. A number of firms are experimenting with special permanent containers to protect small shipments and allow fast handling.

Even buses help hard-pressed traffic managers. More mail-order goods, tractor parts, and other small shipments are moving on its 5,000 intercity buses, Greyhound Corp. reports. Frequently, recipients can pick up parcels at conveniently located downtown bus terminals and save a local delivery fee, and traffic men favor speedy buses for hurry-up orders. ♦

HOW COMPANIES ARE USING

Product Managers

Condensed from Printers' Ink

FOR EVERY COMPANY with more than one product line, today's intensely competitive market poses a special organizational problem: how to put great marketing effort behind each product when there are so many products and markets. A growing number of companies are finding their answer in product managers.

The product management concept offers:

- Concentrated firepower in each market segment, through centralized planning responsibility.
- Greater efficiency through greater liaison and coordination. Current marketing is complicated not only by the growing number of product lines, but also by the growing number of functions (marketing research, product planning, etc.) required for each. The tangled web of activities surrounding a product can often be synchronized by a product manager.
- Increased profitability, through savings from improved efficiency and a stronger position in the market. General Aniline & Film, for example, estimates that its product-manager system has meant millions of dollars to the company in the three years since the system's installation.

Printers' Ink (October 14, 1960), © 1960 by *Printers' Ink Publishing Company, Inc.*

JANUARY, 1961

There seem to be three basic types of product-management organization:

- An advertising (and sales promotion) orientation—most common among consumer companies, like Procter & Gamble, where advertising is such a large and critical part of the marketing program.
- A sales (and technical service) orientation—prevalent in the industrial field, where customer relations and service are paramount requirements. At Du Pont, for example, a PM may report upward through four or five levels of sales executives.

- The general management orientation—the most comprehensive kind, and the rarest. The general manager is found in large companies like General Electric, which has more than 100 product departments or "profit centers," each headed by a general manager responsible for everything about his products from manufacturing to marketing, with supervision from above.

The Advertising Orientation

Kimberly-Clark's consumer division, which has used product managers since 1956, reflects the advertising orientation. The division uses seven brand managers, six handling one

brand each and the seventh two. Their work is supervised by a products manager, who reports to the marketing services manager. Each brand manager is responsible for drawing up complete marketing programs for his brand. But, says a company spokesman, "The brand manager spends 75 per cent of his time on advertising and promotion campaigns—creating, budgeting, and getting approval." There is no divisional advertising department. The brand manager serves as ad manager for his products, working with an account executive of one of the company's two ad agencies.

In addition, the brand manager is responsible for recommending marketing objectives for his brand, planning marketing strategy, drawing up proposed budgets, initiating new projects and programs, and coordinating the work of all functional units concerned with the production, financing, and marketing of the product. He must also maintain communication with management and with the departments working with him, and he must constantly evaluate performance and recommend changes as necessary.

The brand manager has no staff of his own, but may draw on the resources of advertising agencies and the division's sales promotion, budget control, manufacturing, and sales departments. The brand manager has a definite responsibility for the profitability of his line, but no price-making authority and no profit accountability.

The Sales Orientation

The chemical division of Merck & Co., Inc. places its accent on sales and technical service. In the chemical division (one of four divisions

in the company), each of the five product departments has its own sales force. For example, the general products department, which sells a variety of additives to food packers and processors, is headed by a marketing director, who is also the sales manager. This department is composed of two units: sales and product management.

Under the manager of product management are three product managers, handling meat products (meat curing, fermenting, and flavor-enhancing products for meat packers and spice houses who serve packers), enrichment products (enrichment mixtures, bulk vitamins, amino acids, etc., sold to cereal, grain, and baking industries), and food products (citric acids, bulk vitamins, amino acids, etc., sold to packers, canners and the frozen food industry). In addition, there are a technical service manager and one assistant product manager.

Each product manager is a staff member whose primary function is to "plan for the growth and profitability of his markets." The emphasis on markets, rather than products, indicates a growing trend among industrial companies toward serving the needs of their markets rather than simply selling products on hand to various customers. In some cases, the same products are handled by several product managers. It is their job to know their markets thoroughly and to exploit possible uses for the company's products.

The product manager is his own ad manager, working with either of the two agencies that serve the chemical division. Within the division, he may call on a variety of services from divisional departments, including

product development and sales and marketing.

The General Manager Concept

Raytheon uses the product-department general-manager concept. The company has 12 operating divisions, within which departments (called "operations") are headed by "operations managers." Raytheon's government equipment division, for example, has five operations managers reporting to the division general manager. In addition, there is a divisional marketing director, who provides staff aid to operations managers in such areas as advertising, sales promotion, and product planning.

Some operations managers have sizable staffs of their own. For example, the manager of the submarine signal operation has eight functions reporting to him, including manufacturing, engineering, and marketing. The divisional marketing staff assists them, too, but in theory at least, the operations manager makes the decisions.

What is the role of the PM in other companies? The results of a recent survey of 20 large companies or divisions—ten consumer and ten industrial ones, employing 77 product managers in all—provide answers to some often-asked questions:

What are the PM's responsibilities? They vary widely between consumer and industrial companies. Companies were asked to list primary responsibilities of their PM's. All of the industrials listed first, "Recommends additions and deletions to the line"—a reflection of the importance of market needs over product selling. Nine out of ten added sales forecasting and sales promotion. And eight out of ten

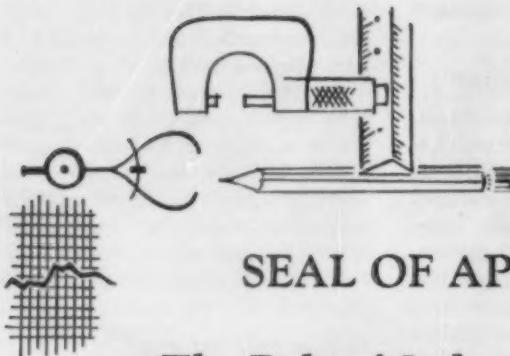
noted that their PM's determine product specifications and participate in sales planning. While all 20 companies noted that their PM's made periodic fact-finding field trips, eight out of ten industrial PM's "assist in selling key accounts"—a function listed for none of the consumer PM's. And all industrial PM's are required to counsel regional or district sales managers, as against 80 per cent of consumer PM's.

Neither Fish nor Fowl

How does he operate? There are many confusions about the PM system, probably resulting from insufficient experience with it. For example, 60 per cent of the consumer companies designate their PM's as line executives, when in fact some of them exercise little line control and actually perform planning and advisory duties usually designated as staff. Probably the most realistic approach to the question of line or staff designation is offered by the two out of ten consumer companies that make no distinction—for they most clearly suggest the fluidity of the situation.

In addition, 60 per cent of the consumer and 50 per cent of the industrial companies reported that they give their PM's "price-making authority." However, almost all added some qualification that dilutes that authority to making serious price recommendations.

What are his reporting arrangements? Generally, the product manager reports to a higher marketing executive. This is more common in consumer companies; among industrials, eight out of ten report to general managers of their divisions. ♦



SEAL OF APPROVAL:

The Role of Independent Testing Laboratories

By Arthur Gregor

Condensed from Industrial Design

ONCE UPON A TIME, when commuters found a red carpet awaiting them as they stepped off a train, it meant that royalty was aboard. But today it is more likely to mean something else: A testing laboratory is using the passengers as guinea pigs.

If so, the laboratory is carefully counting the number of people who set foot on the carpet. A testing team is supervising the carpet's daily vacuuming and weekly shampooing. Back in the laboratory, the carpet is being checked for wear resistance and color fading. Reports are drawn up, data evaluated, and comparisons with competitive products established. Finally, a seal of approval is affixed to the carpet. And in today's market, the seal of approval counts.

Approval may take many forms. It may be the testing laboratory's official

insignia, printed on the product. It may be the tag that says: "Certified washable. Do not boil or bleach." It may be a seal appearing in a corner of a newspaper advertisement, or a label stating the exact composition of a material. Whatever it is—and whether or not the consumer actually stops to read an entire tag or seal—its mere presence on a product is reassuring and influences the buyer. He feels secure in his purchase—and the manufacturer knows that the buyer will prefer an authorized product.

The Designer Is Tested

In the planning stages of a new design, testing may be the least creative phase—but it is in many ways the most critical sequence of operations during pre-production, and even during production itself. What is ac-

Industrial Design (November, 1960), © 1960 by Whitney Publications, Inc.

tually tested is not the product but the designer—the total validity of a design idea and of product planning. What good is an idea if it won't work, isn't safe, and won't sell? However obvious these questions, it is only by testing that they can be answered. It is during this part of product development that omissions in planning become evident and that inaccurate thinking and engineering are detected.

Testing is the confirmation of ideas—its result is data. There are four factors without which the success of a product cannot be guaranteed and for which data must be established. They are *performance*, *certification of manufacturers' claims*, *psychometrics* (the study of consumer response), and *safety*.

Performance and Certification

Performance tests precede all others in product evaluation, for the success of a product's performance is what certification affirms. Most manufacturers have their own facilities for testing performance and endurance, but rely on outside services for their special facilities and for their impartiality in comparing products. Among the performance factors tested, for example, are the wearability of a carpet (via abrasion tests), the vibration of a household mixer (with a strobe light), the heat distribution of a kitchen range (with thermocouples placed on various locations on the range), the brittleness of a new synthetic formulation (in simulated Arctic cold).

Certification testing means policing a product: conducting a continuing monthly audit of a product for performance, economy of operation, ma-

terials, durability, ease of repair, safety characteristics—in short, all the product's end-use characteristics. Certification programs are carried on for such products as home appliances, women's hosiery, socks, cigarettes, skirts, watches, even diamonds.

The Human Response

Psychometrics involves testing human response to products and packages. United States Testing Company, Inc., for example, employs four psychologists, two statisticians, and three home economists, who try to determine not only consumer preferences but also the motives underlying a given choice. At "consumer response centers" located throughout the country, U. S. Testing invites the public to list their choice of appliances, cigarettes, whisky bottles, cereal packages, etc. Appliances are evaluated for appearance and function against competitive products; packages are checked for readability, attention value, apparent size (the effect of labels and designs on the buyer's concept of size), apparent quality (which can of soup costs more and tastes better, judging from the appearance of the package).

Finally, safety tests guarantee that products are not potentially harmful to operate. Underwriters' Laboratories, Inc., for example, affixes their valuable label—or permits manufacturers to do so—after merciless investigation has proved a product to be free of fire, shock, or casualty hazards. To determine a product's fire-security, for instance, UL not only simulates normal in-use conditions but devises abnormal ones. A television set will be run for seven hours at 120

volts, to make sure no failure of any sort will occur. Its glass screen will be struck with a metal ball, to guarantee its implosion resistance. Other tests will include measuring leakage of metal parts to ground for shock resistance and short-circuiting circuit elements to find out if the materials used will catch fire under excessive heat.

Using Outside Facilities

Most manufacturers can run, with their own facilities, the tests necessary to obtain information in these areas. The performance of an appliance, for example, must obviously be tested first in a company's own laboratory and then, as the product rolls off the production lines, in quality control. All the obvious dimensions—electrical as well as mechanical—are, of course, tested by companies without much trouble. Even the most difficult tests—operation at sub-zero temperature or high altitudes, vibration and endurance checks—can be performed by most manufacturers on home grounds. But there are certain performance tests for which companies have neither the equipment nor the time. And of course the validity of self-certification is always open to question. For these more elaborate and/or impartial tests, companies must seek the appropriate outside facilities that serve industry in just these areas.

Manufacturers seek out independent laboratories for three basic types of service: *impartial evaluation, extensive facilities, and safety approval* required by federal and local laws. The impartial status of the independent laboratory makes its findings acceptable to manufacturers, customers,

and inspection authorities. The manufacturer also relies on the laboratory's unbiased attitude when he asks its engineers to evaluate his products against competitive items.

For-Profit and Non-Profit

Like independent R&D services, the testing laboratories are set up either as for-profit businesses or as non-profit organizations sponsored by universities, the federal government, or business groups. One of the largest independent for-profit laboratories is the United States Testing Company, Inc. Its main resources are its immensely diversified testing equipment and systems.

The country's best-known laboratory whose sole concern is public safety—Underwriters' Laboratories, Inc.—is run as a non-profit enterprise under the guidance of a board of trustees whose members are officers of stock insurance companies throughout the nation. This tends to assure impartiality and objectivity—the two major services that any testing laboratory has to sell.

There are many such laboratories throughout the country. The American Council of Independent Laboratories—an association of for-profit groups—lists 78 members in its 1958 directory. Collectively, these laboratories employ several thousand chemists, biologists, engineers, physicists, metallurgists, and technicians. Another directory, "Standardization Activities in the United States," published recently by the U.S. Department of Commerce, lists 350 organizations sponsored by government agencies and various business and/or professional organizations. ♦

**The consumer may be
changing his mind about
what he really needs
and wants . . .**

New Standards for Consumption?

*Condensed from
Business Week*

WHAT HAPPENED to the consumers last year? Why didn't a growing population, growing families, and fat incomes add up to record spending for goods?

To find out what happened—and what is happening—to consumer consumption, *Business Week* researchers in 25 cities have been asking people: What excites you? What do you want? Why aren't you buying? The answers point to a clear warning to

marketers: If you think the customer has been tough to sell up to now, you haven't seen anything yet!

First, Educate the Children

One reason many consumers are not on a buying spree is the cost of rearing and educating children. Schools continue to be a burning issue. Let's not stint, is the verdict. A Worcester, Mass., school board was going to cut out a sprinkler system with the praiseworthy object of paring costs. The parents voted a firm no to that nonsense.

Many communities have graduated beyond concern for plant. It's the caliber of the education offered that worries them now. So they are going into action. "It has gone beyond PTA," says a Detroiter. The thing to do now is to work on the school board and vote in school elections. Elections that a few years ago drew maybe 25 per cent of Detroit's voters are now drawing anywhere from 50 to 90 per cent. In Louisville, the "gifted child" is getting a lot of attention. Some cities—Nashville, for one—are heading for private schools, partly as an aftermath of integration. One New Yorker is so concerned about the caliber of schooling that he teaches some courses in his spare time.

College is a must. The children themselves feel the pressure of competition for the "good" schools. More than one parent fears that education as a panacea is being overdone. Among the better heeled, child care includes all the frills: music lessons, ballet lessons, extra French lessons, and charm schools for young daughters.

Reprinted from *Business Week* (November 19, 1960) by special permission; © 1960 by McGraw-Hill Publishing Co., Inc.

The child has reversed whole patterns of living. Parents are going to church who would be unlikely to go if it weren't for the children. Leisure activities are geared to children's interests.

The elders of this postwar generation are counting the cost, and reaching for the aspirin. Wives are going back to work to pay for Emma's private school. An old car is made to last "till the children get through college." One family gave up its summer home. Another put off buying a boat. People at all levels are scanning the stock listings for a good investment to get Eddie through college.

Why They Aren't Buying

The high cost of a family today goes far toward explaining the let-up in buying. But there is other competition for that tight-stretched dollar. More people are investing against a rainy day or to bolster retirement income. Such investments are untouchable. "We mustn't touch our assets," insisted a 28-year-old Pittsburgh housewife. Clevelanders are strapped; they are buying stocks.

The heavy emphasis on security and investment indicates worry about the future. "If I weren't so worried about the future, I'd be spending more now," a St. Louis newsman reports.

The families who started 12 or 15 years ago and have climbed the economic ladder have a happier reason for slowing down. As one woman put it, "We have about everything we can use. I don't see any real need for anything but luxuries."

From well up the income ladder, a Houstonian summarizes: "We have all had our lunch. We are enjoying

a feeling of satiety. And we aren't ready for supper."

Among the older (and some younger) families, there is a tendency to de-emphasize material possessions—an easy thing to do if you already possess them. There's some feeling that consumption for consumption's sake is palling. The attacks of the reformers have been read, noted, and possibly are having some impact. Vance Packard's *The Waste Makers*—a book that attacked consumption—is a bestseller.

In some quarters, a half-hearted revolt is under way. "I'm sick of being told to buy," says a Milwaukeean. A Pittsburgher argues, "No one can convince me that you have to trade in your car every two years." And from a New Yorker, "We have too many possessions. We're throwing our furniture away."

Call it a mature market—mature in ownership, wise in the ways of buying. Since many postwar families are buying mainly for replacement, they can take it easy. They shop, look at price tags, read labels. They don't have to buy a new chair today; they'll spend freely enough when the time comes. But what they buy had better be good—and it had better be better than what they had.

The Better Life

The sophistication that has come with years of buying has even begun to cause some doubt about the beauty of installment buying. An executive says, "I don't have the money to buy and I don't want to go into debt any more." The feeling that it isn't quite right is growing—and besides, it costs more.

Ask them what they want, and most people come up with a recognizable version of the good life—20th century style. What this is, of course, depends on where you stand in the economic and social scale.

For the common people, one theorist has it, the good life means security; for the rich, that something extra that no one else has; for the in-betweens, affection, comforts, a

chance for the kids, and a little left to spare. For the young adults, adds another, it's stability—which means early marriage, early home buying, a chance to do something responsible.

Most of the targets translate into specifics, into terms of good goods. But there is one exception: happiness for the kids. "I don't care what my boy does, just so he's happy. If he wants to run a gas station, let him." ♦

Who Handles Ad Inquiries Best?

MOST FARM-PRODUCT ADVERTISERS answer their advertising inquiries within ten days. Industrial and consumer advertisers take a little longer, but they do a better job on other phases of inquiry-handling.

These, reports *Industrial Marketing*, are some of the findings in a survey conducted by Potts-Woodbury of Kansas City, Mo., of the inquiry-handling practices of advertisers in three distinct types of publications: a consumer magazine (*Better Homes and Gardens*), a farm publication (*Farm Journal*), and an industrial publication (*Practical Builder*).

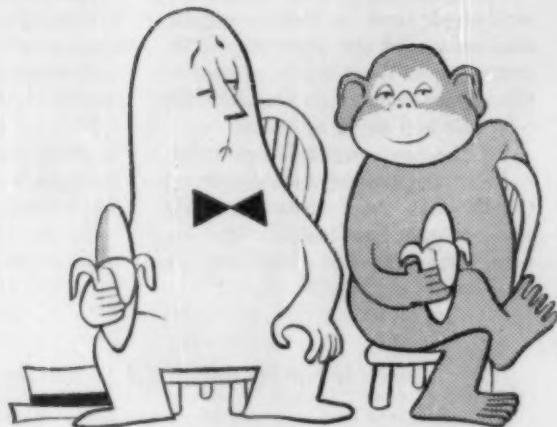
Median time for reply by farm paper advertisers was ten days; for industrial and consumer magazine advertisers, twelve days. But industrial and consumer advertisers had better records in including covering letters in their replies: 63.2 per cent of industrial advertisers, 53.1 per cent of consumer advertisers, and 48.9 per cent of farm advertisers enclosed letters.

Other highlights of the survey:

- Industrial advertisers did best in personalizing replies: 67.3 per cent of them did so.
- Consumer advertisers did best in including brochures with their replies: 93.8 per cent did it, compared with 83.3 per cent of farm advertisers and 52.9 per cent of industrial advertisers.
- About 75 per cent of all advertisers did not tell how or where to buy their products; of those that did, only 40 per cent named a local source.
- A small percentage of advertisers failed to reply to the inquiry at all: 15.8 per cent of consumer advertisers, 11.7 per cent of industrial advertisers, and 9 per cent of farm advertisers.

On the basis of its survey, Potts-Woodbury offers three pointers on handling ad inquiries:

- The problem of handling inquiries should be considered—and budgeted for—in conjunction with every advertising program.
- A system should be established to insure prompt answers.
- Every response should tell the prospect how and where to buy.



EMPLOYEE SELECTION: How Valid Is Personnel Testing?

Condensed from Industrial Relations News

OVER THE PAST TEN YEARS, there has been a strong growth in the use of formal testing programs for job applicants. A survey of 852 companies by the Bureau of Business Research of the University of Texas found that 80 per cent were using tests of one kind or another to measure the capability of job applicants, compared with only 57 per cent a decade earlier.

This growth is reflected by the firms that sell test services to industry. Lyle M. Spencer, president of Chicago's Science Research Associates, Inc., reports that his business clients now number about 11,000—triple

the 1949 figure. And Dr. Harold Seashore, vice president and director of the test division of The Psychological Corp., New York, reports an increase in test sales that will help push his company's revenues up close to \$3 million this year, compared with less than \$2.7 million in 1959.

Despite this evidence of solid and consistent expansion, there remains a group of executives who still have some doubt about the usefulness of tests in employee selection and upgrading. Recently, the president of a Chicago executive-placement agency said flatly: "In my opinion, they are utterly worthless."

Industrial Relations News (November, 1960), Industrial Relations Newsletter, Inc.

The greater weight of evidence, however, indicates that tests are worthwhile indeed—provided they are properly conceived and administered and their results intelligently evaluated. But there are pitfalls that can interfere with maximum dollars-and-cents payoff.

The first thing to avoid in reviewing or installing an employee testing program is reliance on test results alone to reveal whether a man is equipped to do a specific job. A psychological test, for example, doesn't necessarily measure a man's learning ability, and a learning ability test doesn't necessarily measure how well a man follows orders. Tests, then, can be properly used only in conjunction with other methods of appraisal.

Other Appraisal Methods

Chief among other methods is the standard employment interview. This, together with a careful check of references, can provide a fairly comprehensive portrait of the employee. The test battery can be used to define areas for further probing, or to check the reliability of other findings. Covington Shackleford, manager of industrial relations for the National Aniline Division of Allied Chemical Corp., cites three immediate advantages of adding a test battery to his division's selection and appraisal program:

- The test series (measuring mental ability, personality adjustment, and vocational interest) helps overcome any weaknesses in interviews or reference checking.
- Selections are made with more confidence.
- Tests cut down on costly inter-

viewing time by revealing specific areas to investigate.

Developing and Testing Tests

There are, literally, thousands of different tests available for purchase by business organizations. Before any of them can be fairly used, you have to know two things: Precisely what are you trying to test, and how well do test results match on-the-job performance?

This is not a simple matter. In 1948, Standard Oil Co. of New Jersey began a program to develop valid test batteries. The program, under the direction of Richardson, Bellows, Henry & Co., New York management consultants, first determined what attributes management believed most important to job success. Then tests were devised to measure these characteristics precisely. Finally, follow-up performance reviews were compared with test results to see if the test findings proved out.

The validating of tests is a continuing process. When the effectiveness of selection drops off, it's time to review your test battery. One company was using an arithmetic test to help select accounting clerks. But the test lost its validity when the accounting department operation was mechanized, and a different type of skill was required.

The Test Administrator

A test is only as good as the man who administers it. For this reason, most testing authorities insist that the person who administers and evaluates tests must be specially trained. Highly sophisticated psychological tests, for example, should be handled only by

psychologists. The Psychological Corp. has a staff of three people assigned to checking qualifications of those who want to buy such tests.

There is, however, some controversy in the testing field about just what tests can be evaluated by whom. Allied Chemical's appraisal program includes a personality test that is evaluated without the help of a psychologist. The test was developed by Clark, Channell, Inc., a Stamford, Conn., consulting firm that offers a three-day seminar to train personnel administrators in using it.

One important thing to remember is that the person who makes the overall appraisal of the applicant should not be the one who makes the hiring decision. In this way, objectivity is maintained, and the individual is protected from exposure of personal information that may have no bearing on his ability to fill the job in question. For the same reasons, psychologists don't hand out specific test scores, but present their findings in written report form.

The Ethics of Testing

The exposure of personal information in connection with psychological and personality tests causes some critics to ask whether they constitute an invasion of privacy. Proponents say there's little danger of this if they're handled by trained administrators, equipped to evaluate them properly. Here's an excerpt from a memorandum put out by the medical division of the Caterpillar Tractor Co.:

"Psychological information is confidential and should be treated as such. . . . Interpreting test information in

many instances runs the danger of 'tagging' a person for life and could greatly affect his emotional health. Therefore, psychological interpretations should be made only by qualified, trained persons who know what should be said and what is better left unsaid to the individual. It should be kept in mind that test data are only one aspect of a person's qualifications."

Measuring the Payoff

There is enough positive evidence to indicate that a well-conceived test battery can sometimes have spectacular results. One company, for example, decreased its turnover rate from 54 per cent to 31 per cent over a six-month period with the help of an interest-inventory test. This kind of result, of course, can be measured in dollars. Just saving the expense of training ten salesmen, for example, might save a company \$20,000. Another company devised a testing program that enabled it to quickly staff a complete plant at one-third the anticipated cost.

Nevertheless, experts emphasize, it's hard to isolate the results of tests in turnover. One executive development director found that such diverse factors as the season of the year and the success of the company affect the turnover rate.

Generally, psychological tests are used to weed out employees who are expected to fail rather than those who will succeed. Says Walter Ronner of Budd Lewyt: "I've seen supervisors who have done well on tests but didn't make good. But I have never met a supervisor who failed and made good." ♦

SCRAP, WASTE, AND SPOILAGE:

Dollars Down the Drain

By Donald E. Patterson

Condensed from The Price Waterhouse Review

ABOUT 20 per cent of all iron, steel, aluminum, and copper that go into production comes out as scrap—and the cost of this waste can run as high as a million dollars annually in some companies. Much of this loss is avoidable. In fact, a well-defined and well-managed scrap control and disposal program can often have a greater effect on company profits than can increased sales—and without capital risk.

Whose Responsibility?

Providing protection against losses arising from scrap, waste, and spoilage is an important part of management's responsibility. Although some spoiled work is inevitable, defective work does not just happen—it is caused. It may be due to carelessness on the part of machine operators, inadequate supervision of factory employees, the use of defective materials or the wrong materials, faulty equipment and tools, or errors in product design and processing. This list does not include all possible reasons, but it indicates the wide area of responsibility for reducing losses resulting from defective work.

The quality of workmanship is, of course, within the jurisdiction of the

production supervisors and foremen. The condition and types of raw materials and parts used are the responsibility of several departments, including engineering, procurement, materials handling, and inspection, as well as the production departments. The production, engineering, and maintenance personnel are responsible for the nature and condition of tools and equipment used in production. The engineering department must also assume responsibility for product design and processes. The salvage department's duties include the collection, segregation, reclamation, and disposal of scrap and waste, but this department, too, ought to be instrumental in reducing the amount of scrap loss.

This wide range of responsibility points up the need for definite assignment of individual responsibility and coordination of effort. And it emphasizes the necessity for adequate records and analyses of the cost and causes of defective work and scrap.

Establishing Controls

Cost analyses usually do not probe deeply enough to expose and evaluate the several causes of defective work and scrap losses. Furthermore, it may

The Price Waterhouse Review (Autumn, 1960). © 1960 by Price Waterhouse & Co.

be many days or even weeks after the losses have occurred before the analyses are available for use. In order to track down the areas and eliminate the causes of such losses, cost analyses have to be coupled with good statistical quality control on the production line. And control of quality is obtained largely through the control of spoilage.

In establishing controls or in expanding existing controls, management must exercise sound business judgment in weighing the relative risk against the cost of the controls. The required degree of control will depend on the company's operations and the nature and causes of its defective work and scrap losses. This can effectively be determined by special studies by production engineering, production control, and accounting department representatives, working together as a team.

Finding Trouble Areas

Comparisons of the company's operations with those found in similar plants and comparison of its scrap-generation ratios with the average for the industry may prove helpful in evaluating controls over scrap. Such comparisons will not, however, prove that the controls employed are either adequate or inadequate. If the company's accounting system already provides for scrap, spoilage, and rework reports, they must be studied and analyzed to find sources and causes of loss. In some cases, the production, salvage, and rework operations and the scrap itself may have to be physically inspected and studied. Finally, costs must be analyzed by the major types of defects found. Such special

studies will indicate the areas in which controls should be strengthened. They may also indicate that greater use of sampling techniques for quality control and inspection will be sufficient in other areas, where scrap and rework are not excessive.

Elements of Control

As in any system of internal control, the procedures established are more likely to be carried out effectively if they are expressed in writing for each department concerned. The procedures must provide adequate accounting control over the volume of scrap and rework by requiring reports of the quantities and types of scrap created, the amounts of and reasons for rework required, and the physical disposition of scrap.

Defective materials and spoiled work sent to the salvage department should be accompanied by tickets or reports prepared at the point of generation. For accounting control, such reports should be prenumbered and should show not only the quantity and description of items, but also the source and cause of rejection. After the scrap or salvage department has physically checked the quantity and indicated its disposition on the ticket, the original report should be sent to the cost department for pricing and then routed to general accounting. At the time of initial preparation, copies of each ticket or report may be directed (a) to the general accounting department for control, (b) to the production control supervisor or plant manager for information and possible investigation, and (c) to the responsible department foreman. The specific manner in which the reports are

handled will, of course, depend on the nature of the company's manufacturing, salvaging, and accounting routines.

The reports of scrap and rework quantities should be summarized periodically and, where possible, related to product yield. Where there is some uniformity in particular operations, the quantities of normal or inevitable scrap and rework can usually be predetermined and anticipated, and standard factors can be developed and used to check on the reported rework and scrap recoveries.

Segregation and Reclamation

It is also important to have a physically segregated salvage and scrap area and regular collection and disposal procedures. All spoiled material should be sorted and classified on the basis of the ultimate disposition expected. Some may be reclaimed and returned to stores, some may be profitably reworked into saleable products, and other portions will ultimately be disposed of as scrap.

The procedures must provide physical control over scrap leaving the plant. All scrap should be weighed or measured in some manner at the time of its removal from the plant, and all disposals should be reported direct to the accounting department for control over billing and receipt of payment.

In addition to adequate physical control over scrap, the procedures established should provide methods for obtaining maximum dollar realization. More dollars can be obtained from scrap that is properly classified and segregated by basic material content and is relatively free of contami-

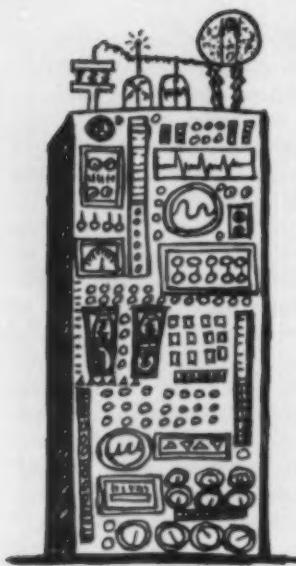
nation. There is a large variety of specialized equipment for reclaiming and conditioning scrap — such as pressing and baling machines, centrifugal machines for removing contamination, etc.—which can help add to the sales realization value.

Every means of using the rejected materials should be considered in order to avoid dollar loss through the sale of usable materials as scrap. On the other hand, no rework should be authorized without first considering production requirements and relating the rework costs to realizable values. There is always a possibility that rework cost, when added to costs already incurred, may exceed the product value recovered, and more profit may be realized or less loss incurred if the defective item is sold as a second or scrapped.

Disposal of Scrap

To be sure that the company is receiving the highest possible prices for its scrap, relatively frequent competitive bids should be obtained from appropriate, qualified scrap dealers. Consideration should also be given to the possibility that the vendor from whom the material was originally purchased might offer a better price than a scrap dealer. In any instances where scrap has resulted from existing defects in purchased materials, every effort should be made to obtain full credit from the vendor.

Trash and waste disposal, as distinguished from the sale of scrap, should also be contracted after competitive bidding. However, realization of cost savings in this area must, by and large, come from control of the amount of waste. ♦



Next, the Solid-State Vice President

By George A. W. Boehm
Condensed from Fortune

A MAJOR and long-awaited breakthrough in automation has taken place: Machines soon will be able to make operating decisions on their own and act on them, allowing complete automation from the production line on up.

Several companies, including Texaco, Louisiana Power & Light, and Republic Steel, have already installed computer process control (CPC) to take charge of some of their production processes. The CPC machines provide the "missing link" in the chain of electronic computers that can integrate decision-making through all of a manufacturer's major operations: purchasing, production and production scheduling, inventory con-

trol, distribution, marketing, and perhaps even finance. In time, when the links are joined, the computers that control processes will work together with business-data computers to make routine decisions all along the line, up to the vice president's office.

How CPC Works

CPC is being launched by companies that have already replaced most of their labor force with machines and automatic controls. But it promises no additional payroll reductions. On the contrary, it is expected that in most cases all the human operators will be kept on the job as standbys in case of emergency, and, in some instances, at least one extra maintenance man will be needed to service the computer.

Maximum operating efficiency at

Fortune (December, 1960), © 1960 by Time, Inc.

all times, through better and faster decision-making, is what the computer offers. A computer can make a running analysis of the process and compensate for changes as fast as they occur. Connected by its own communications network to perhaps hundreds of instruments, the machine gathers, in rapid succession, reports on critical variables in the process. The computer then analyzes how things are going. It takes a computer's fantastic speed to analyze what is happening in, say, a steel-rolling mill where strip is flashing by at nearly 35 miles per hour, or in a chemical plant where thousands of calculations must be made to reveal the exact state of the process.

After analysis, the computer makes decisions, calculating how valves, burners, rollers, and other apparatus should be adjusted. Finally, it takes action. It dispatches back through the communications network a series of commands that cause individual controls on each piece of apparatus to make the necessary adjustments. And it can repeat this routine hundreds of times a day for weeks at a stretch, virtually without human supervision. In its spare time the computer can type out a condensed log of the operation.

Bury and Forget Them

What sets the control computer apart from most business and scientific computers is its phenomenal reliability. The CPC machines are built almost entirely of solid-state components, and each component is individually tested. They are guaranteed to work for more than 99 per cent of the time, and those that are now

controlling processes are meeting this guarantee easily. Chalmer Jones, general manager of Daystrom's Control Systems Division, thinks they can be made even more nearly fail-proof. He says, "I'm sure in 15 years we will build computers so reliable that you can bury them in concrete and forget about maintenance."

Computers on the Job

CPC is getting its start in four basic industries: electric power generation, steel rolling and plating, petroleum refining, and chemical manufacture. Though they may seem disparate, their processes are similar in one respect: In all of them, energy and materials flow continuously, almost without interruption. Continuous processes readily lend themselves to mathematical formulation, without which a computer cannot be programmed to take over control.

Different processes put different demands on a computer control system. In the chemical and petroleum industries, the control computer's chief duty is to make an enormous number of calculations. The computations are so involved that even a high-speed computer may take several minutes to come to a decision. Fortunately, chemical and petroleum processes are relatively sluggish and need not be adjusted frequently.

The cost of a process-control computer and the communications network it requires, plus engineering studies and extra instrumentation, generally runs from \$200,000 to \$1.5 million, depending on the complexity of the process. But a company can achieve CPC by stages. Many companies have started by using com-

puters off line: Human operators have remained in complete control of the process, with engineers using a computer to make studies of control systems. Other companies have put computers on line, but not in control. These are linked to the process to do the monitoring and print out analyses that serve as operating guides for human operators.

Whatever the costs, reliability and increased production efficiency are what manufacturers pay for. Many processes with annual outputs from \$3 million to \$30 million now fall short of maximum theoretical efficiency by 15 per cent or more. If better control picked up most of this waste, the extra production would pay for a computer in short order.

Accuracy and Economy

CPC also makes possible more accurate production scheduling, and this in turn may enable companies to economize on inventory. James N. Madigan, development scientist of B. F. Goodrich Chemical, stressed this point at a recent technical conference: "It is not unusual in the chemical industry to keep an inventory of one month's supply of a product or chemical intermediate. For a 20-cents-per-pound product produced at five million pounds per month, this is a capital investment of \$1 million. If this could be cut 25 per cent with the same capacity for meeting changing market conditions, the capital investment in the computer system would be balanced, and the other benefits would be pure profit."

Increased safety and reliability are another plus that CPC offers. They are especially important for the power

industry. "The penalty for a single error in judgment is becoming financially prohibitive," says engineer William A. Summers of Ebasco Services, Inc., the engineering company that is installing CPC for Louisiana Power & Light and Carolina Power & Light. Summers estimates that one in three big generating units suffers a major accident some time during its operating lifetime. Each accident causes about \$1 million worth of damage on the average and puts the unit out of commission for two to four months. At \$8,000 per day, this piles up to an operating loss of \$500,000 to \$1 million. Summers believes that a carefully programmed computer should be able to cope with emergencies more surely than a harried operator. In his opinion, safety procedures alone amount to a form of insurance that will pay for about half of the whole CPC installation.

Anticipating Trouble

Given fast-acting instruments and controls and the split-second decision-making of a computer, engineers are beginning to apply a much more sophisticated form of control: "dynamic control." Today's CPC systems are designed chiefly to maintain a process close to some economic equilibrium, and controls are usually readjusted only *after* changes occur. With dynamic control, the computer would note a fluctuation at one stage of the process—say, a sudden rise in temperature—anticipate the possible effects on the next stage, and take steps to compensate for the fluctuation *before* it affected the second stage. However, dynamic control of all processes is probably a long way off. ♦

What's Wrong with PR Overseas?

By Charles E. Allen

WHAT HAPPENED IN CUBA is a painful reminder of the power of public opinion to damage U. S. business interests abroad. The Castro regime has used "Yankee imperialism" as a popular devil to strengthen its support among the Cuban people. And the Cuban public, showing little understanding or appreciation of American business, has largely applauded the government's actions in taking over U. S. enterprises.

It might be comforting to chalk off the Cuban situation as an isolated development. But there are abundant signs of incipient Castroism elsewhere in Latin America and in other underdeveloped areas of Asia and Africa where U. S. business has substantial investment. Moreover, there is disturbing evidence that American business has real public opinion problems even in highly industrialized countries that have close political, economic, and cultural ties with the United States.

Common Defects

Many American public relations activities abroad share important defects:

1. Lack of clear public relations policy. Many companies have not analyzed their basic public opinion prob-

lems adequately and determined what should be done about them and who should do it.

2. Over-reliance on line management to cope with the intangibles and complexities of public opinion. Nationals in line management usually have little knowledge of public opinion and communications techniques. Americans generally lack sufficient knowledge of the foreign environment, and often fail to adapt U. S. public relations techniques to the specific conditions abroad.

3. Underrating the public relations function. When an American company does employ qualified international public relations assistance, it often buries the operation deep in secondary management.

4. Over-dependence on marketing techniques, especially product advertising and publicity, to deal with public opinion matters. This confuses two quite different problems—the selling of tangible products and the explanation of the company itself. The citizenry is interested in, and often worried about, such things as the company's impact on the local economy, its policies for developing local managerial talent, and its contributions to the country's economic development and social progress.

Condensed from an address before the Business Council for International Understanding,
The American University, Washington, D.C.

These are not items that can be "sold"; they are questions that are best answered by responsible corporate behavior, effectively communicated.

5. Talking too much and not listening enough. There are often substantial differences between what the company wants to say to the public and what the public wants to hear. When people grow tired of being talked at—but not listened to—they simply disregard the company's efforts as propaganda.

Tackling the Job

How does top management tackle the public-opinion job? It should begin with an analysis of the company's public-opinion situation in its principal operating areas overseas. This analysis requires a clear definition of the various groups that are interested in—and essential to—the company's success: the company's employees and their families; other residents of communities where the company operates; local, regional, and national government; the company's shareowners and prospective investors; customers and prospective customers; licensees, dealers, and distributors; suppliers; the business and financial community; and communications media.

Representative samples of each important group should be interviewed to determine:

- What proportion of the group knows of the company, what the company does, what products it makes.
- What these people think about the company's policies and products.
- What they would like to see the company do in the future.
- Where they get their information and impressions about the company.

Such an audit may answer many questions that lie in the area of company policy:

1. Has the company created sufficient national participation in the enterprise? This involves such matters as issuing stock in a foreign subsidiary for local investors, having major sectors of public interest represented on the subsidiary's board, and staffing its top management with nationals.

2. Is the company making an adequate contribution to the host country's aspirations? This involves contributing to economic development by doing locally as much manufacturing, purchasing, research, and other activity as can be economically justified, and involves encouraging the growth of supplier industries. It also embraces contributing to social progress by assisting local communities to develop better educational, medical, and other public services.

3. Does the company have a satisfactory policy for recruiting, training, and promoting nationals?

4. Does the company have an effective program for selecting and training Americans sent abroad?

Government Relations

5. Does the company conduct its relations with host governments skillfully? How far can the company promote its economic self-interests and support broader measures for improving local economic and social conditions, without becoming a partisan target in domestic politics?

6. Does the company cooperate effectively on broad policy matters with other companies, and with U. S. government agencies? Can—or should—the company work with foreign or

other American companies in the same industry to develop favorable governmental and public opinion toward their activities?

Developing a Program

Considering these questions does not necessarily mean that American companies should change their present policies just because of public opinion. Other considerations may be of equal or greater importance. Certain highly integrated international companies, for example, might lose some flexibility in pricing, scheduling production, and handling earnings among their national subsidiaries if local interests acquired substantial equities in the subsidiaries.

Once all these factors are weighed, the next step is to develop a written public-relations program. It will usually include the following elements:

1. A statement of the company's public opinion situation in each country: a definition of the environment in which public relations must operate and of the main problems and opportunities that must be dealt with. These may include such matters as inadequate recognition of the company, misconceptions about its role in the local economy, and pressures for discriminatory treatment.

2. Establishment of specific public relations objectives. The public relations objective with respect to marketing, for example, can specify the favorable attitudes that need to be created among customers and prospects. Other public relations tasks may cope with major political and economic issues that affect the company's ability to operate efficiently.

3. Development of public relations

activities designed to advance the company's objectives. These might include trade exhibits, industrial safety programs, scientific conferences, technical training schools, and support of education and culture. An oil or motor company, for example, might promote projects for improved roads and highway safety. A chemical or agricultural implement company might establish experimental farms. Such economic development is not only in the public interest; it is also in the company's long-range economic interest.

Reaching the Public

4. Effective communications to the public, through defined channels. The general public can be reached through mass media, especially on matters of general interest. Specialized media such as trade journals can carry more detailed information directly to specific groups. The company can develop its own media to communicate with important groups that cannot adequately be reached through existing media. These media include special publications for employees, prospective employees, dealers and distributors, customers and prospects, and sometimes local communities.

5. Adequate resources to carry out the program: details of the manpower and financial requirements, of the composition and responsibilities of the public relations firm, and of the costs for each activity.

6. Evaluation of the program's effectiveness: periodic comparison of performance against objectives and in relation to costs—to keep the public relations program adapted to changing circumstances. ♦



CONVENIENCE— Newest Necessity in Packaging

*Condensed from
Modern Packaging*

TO DAY the most important word in consumer packaging is "convenience." Phrases like heat-and-eat, cook-in, and boil-and-serve dramatize a concept now sweeping far beyond the food field into every product category. Easy-opening devices and other package refinements once regarded as extras are rapidly becoming today's "musts."

The strongest justification for the cost of convenience packaging—aerosol sprays, squeeze-bottle window cleaners, pre-measured detergents,

ready-to-serve baby and pet foods—is the fact that the American housewife is no longer a slave to the kitchen. An estimated 18 million housewives hold jobs outside the home. To them, time is money, and their earnings in factory or office more than offset the extra cost of convenience items that save limited housekeeping time. In addition, the non-working housewife places great value on the leisure time that enables her to lead a fuller life through civic, school, and church activities.

Consumer Complaints . . .

That housewives want convenience packaging is revealed in almost every

Modern Packaging (November, 1960), © 1960 by Modern Packaging Corp.

consumer survey. Of nearly 5,000 housewives asked to tell food manufacturers and processors how to make their products more useful, 60 per cent said: "The product is good, but do something about the package." About 24 per cent want something done about package sizes to fit the needs of today's families; approximately 13 per cent are asking for smaller sizes, while 8 per cent want larger sizes to serve larger families; the remainder want package sizes that are more convenient to fit on cupboard shelves.

... And More Complaints

Complaints about packages that are hard to open, hard to empty, or hard to reclose were registered by 19 per cent, who mentioned specifically glass containers, frozen-food containers, spice and coffee cans, bread wrappers, and flour cartons. Improved labeling and direction copy were wanted by 10 per cent, and 7 per cent want greater package durability: spice cans that don't rust, more cereals in aluminum foil, frozen-food wraps that don't get soggy, sturdier packages for baked goods and cookies to reduce product breakage.

Ten Ways to Convenience

There are ten conveniences that must be considered when analyzing packaging:

1. *Convenience of product form.* Whether the product is solid, liquid, paste, granular, cake, or tablet obviously affects the manner in which it is packaged. Often a change in product form leads to new package convenience: Pushbutton containers for whipped cream and foam shaves

were possible only after the products were processed so that they could be pressure packed. One of the next big convenience developments, some observers say, will be the new low-temperature drying process (dehydro-frozen products). Foods packaged in this form are convenient to store and are prepared simply by adding water. Dehydrofrozen baby foods already are on the market.

2. *Convenience of selection.* A package designed to ease a shopper's choice helps lead her quickly to a specific variety or brand. Examples are packages for Sylvania's electric-light bulbs—color-coded to distinguish different wattages—and transparent packages that show off their contents. And packagers are constantly developing improved graphics that instantly tell the shopper what a package contains and how the product can be used.

Package Size

3. *Convenience of quantity or unit.* Package sizes must meet consumer requirements. For example, in metropolitan centers, where there are many small families and live-aloners, the big demand is for small-quantity packages. In suburban areas and small cities, where families are larger and shopping trips less frequent, the larger sizes are more in demand. The packager, however, must be prepared to satisfy all shoppers if he wants to remain competitive.

Packagers must also decide whether they can offer greater convenience via single-use and single-service packages. Ovaltine, for example, regularly in a glass jar, is now being market-tested on the West Coast in a carton that

holds 12 foil-paper pouches, each one containing just enough for a single use.

Open, Sesame

4. *Convenience of opening.* According to most consumer research, nothing is more irritating to women than packages that are difficult to open. One new easier-opening feature that could make the can opener obsolete is a tear-out aluminum top on a low-cost foil-and-paperboard rigid can, now being market-tested for Minute Maid frozen orange-juice concentrate. A simple pull on an aluminum tab, which is welded to the aluminum can end, instantly removes the top. The device is equally applicable to an all-metal can. Other easy-open features are the cellophane tear tape, used on baked goods, paper napkins, cheeses, and pre-packed vegetables; the twist-type bottle cap for jams and jellies; and the screw cap for glass-packed baby foods.

5. *Convenience of reclosure.* Just as they want packages that are easy to open, women want packages that are easy to reclose if the contents are not consumed all at once. They want more screw caps; they continually complain about film packages—particularly for baked foods—that have no means of reclosure; and they would like to store products in cans, if the cans could be reclosed.

6. *Convenience of simple directions.* Simple, large, legible, printed directions—for using the product and the package—should never be overlooked. The most efficient package is self-defeating if the housewife prefers slitting it open with a knife to plowing through the printed directions.

7. *Convenience in use.* If a product is to be used all at one time, then nothing more than easy opening and easy emptying is required. But if the product has to be measured out in small quantities, the package must be designed to make the dispensing easier. For this reason, more and more packages are now equipped with their own measuring caps, pour spouts, brush and sponge applicators, shaker tops, roll-ons, and other devices. But the dispensing device must work. Millions of dollars have been spent on trick dispensers that never get off the ground. A device should offer true consumer convenience and not be just an irritating gadget.

Handling and Storage

8. *Convenience of handling.* The increasing number of glass and plastic bottles with "wasp waists" indicates that packagers are meeting consumer demands for packages with a safe grip. New shapes are also providing sturdy bases that don't tip easily. If packages are large and heavy, carrying handles are being provided more frequently.

9. *Convenience of storage.* Tall containers may create better shelf impressions, but if they don't fit on shelves and in refrigerators, consumers don't like them. And consumers prefer the convenience of storing things in the original package without transferring them to another container.

10. *Convenience of disposability.* Packages that are easy to get rid of when empty are appreciated by consumers. This is part of the reason for the popularity of paper packaging, the no-deposit bottle or can, and plastic packages. ♦

ALSO RECOMMENDED

BRIEF SUMMARIES

of other timely articles

GENERAL

FASTER IN-AND-OUT TOP JOBS. *Business Week* (330 West 42 Street, New York 36, N.Y.), November 26, 1960. 50 cents. Turnover rate among chief executives is increasing in many companies—and is so high in some that there's hardly time to get portraits hung in the board room, according to surveys by *Business Week*, McKinsey & Co., Inc., and Booz, Allen & Hamilton. Reason for the fast turnover: More and more executives are observing compulsory retirement policies, and successors are in their 50's and 60's. Although some object to fast top-level turnover on the ground that a short-term chief has little chance to exert effective leadership, other executives point out that retirement at the top, activating promotions on lower management levels, provides incentive for younger executives and brings in fresh thinking.

WHAT MANAGEMENT SHOULD KNOW ABOUT CORPORATE ACQUISITIONS AND MERGERS. By George D. McCarthy. *The Price Waterhouse Review* (56 Pine Street, New York 5, N.Y.), Autumn, 1960. Gratis. Based on a study of many recent corporate acquisitions and mergers—and the problems and difficulties they presented—this article offers guidelines to businessmen planning to merge with or to acquire another company. It advocates the formation of an acquisitions committee, and tells how to use market price, potential earnings, capacity to pay dividends, and net assets in valuing a company. Also discussed is a fair price,

the method of payment (cash or securities), federal income tax aspects, accounting aspects, and filing requirements with the Securities and Exchange Commission.

CONVENTION FACILITIES ISSUE. *Sales Meetings* (1212 Chestnut Street, Philadelphia 7, Pa.), November 18, 1960. 50 cents. Designed for executives who plan conferences, conventions, exhibits, and shows, this annual issue provides a reference volume on convention hotel and auditorium facilities in North America and nearby islands, and on sources of services and suppliers for meeting and exhibit needs. With the rates provided for meeting rooms, bedrooms, meals, and exhibit areas, you can make a quick estimate of major meetings costs at the sites you are considering. The data are updated, revised, and expanded, and information is provided on airlines and railroads that serve each of the 900 hotels listed in the guide.

IS NOW THE TIME FOR YOU TO CONSIDER A COMPANY PLANE? *Management Methods* (22 West Putnam Avenue, Greenwich, Conn.), October, 1960. Reprints 50 cents. This article can help you to decide whether you could profit from an owned or leased plane, how to choose the right plane, how to "manage" a company plane, when and when not to fly, whether you need a pilot and how much to pay him, how to determine hidden costs, how

Please order directly from publishers

much insurance to carry, and how to depreciate a plane for tax savings. Also provided is a table giving costs and performances (salary of pilot, average price of plane, cruising speed, range, passenger seats, annual operating costs, and cost per seat) of 16 business aircraft.

EVALUATING PROJECT ECONOMICS. By Thomas C. Stout and John W. Weber. *Automation* (Penton Building, Cleveland 13, Ohio), December, 1960. \$1.00. Consider proposals to invest funds in prospective projects in the

light of these basic economic questions: What is the cost of capital that will be needed? How can returns from a project be evaluated relative to the investment required? From a group of unrelated possible projects, which project will be the most profitable? Illustrating specific problems in these areas, the authors show how they are solved and give a detailed discussion of three techniques used to indicate project returns: (1) simple payback, (2) simple return on investment, and (3) time-adjusted rate of return.

INDUSTRIAL RELATIONS

MECHANICS OF CONDUCTING A MERIT REVIEW PROGRAM. By Philip M. Oliver. *Personnel Journal* (P.O. Box 239, Swarthmore, Pa.), November, 1960. 75 cents. Lockheed Missiles and Space Division has a new method for handling merit increases that takes only half the time required by their previous method and shows a saving of over \$50,000. An outstanding feature of their annual review program is the use of IBM cards, which provide space for three levels of management recommendation and contain information about the employee's salary progression, the size and frequency of previous increases, and the relationship of the employee's salary to that of his superior or his subordinates.

THE QUICKENING PACE OF ENGINEER RECRUITMENT. *Industrial Relations News* (230 West 41 Street, New York 36, N.Y.), October, 1960. \$1.00. Since demand for the relatively small supply of engineers and specialists is increasing, companies must improve their technical recruiting efforts. This review of the latest thinking on technical manpower recruiting offers several helpful suggestions: (1) Don't promise the moon—the complaints of one dis-

pointed engineer can quickly spread through the grapevine; (2) insure the technical man's status—some companies are setting up scales equating titles and salaries for specialists and management personnel; (3) send only trained recruiters to college campuses, but don't try to hire only the "cream of the crop"; and (4) use only believable ads.

PROS AND CONS OF INSURANCE AND SELF-INSURANCE OF HEALTH AND WELFARE BENEFITS. Published by the Foundation on Employee Health, Medical Care and Welfare, Inc. (477 Madison Avenue, New York 22, N.Y.), \$1.00. The major emphasis of this report is on the economics involved in comparing self-insurance and carrier insurance; it not only shows how the cost of insured and self-insured benefits can be figured (including premium taxes, commissions, reserves, and administrative and all other expenses), but also supplies detailed worksheets that can be used in making the comparisons. Although concerned primarily with jointly administered funds, the report's findings and recommendations are equally useful to employer or union purchasers of health and welfare benefits.

Please order directly from publishers

MARKETING

FOOD PACKAGES AS HOUSEWIVES SEE THEM: Parts I, II, and III. *Sales Management* (630 Third Avenue, New York 17, N.Y.), October 21, November 4 and 18, 1960. Reprint, complete set, \$1.00. A survey of 1,098 housewives on food packaging reveals their attitudes, opinions, likes, and dislikes. Packaging does influence their food-buying habits: They like efficiency and convenience and have little use for products that don't give it to them. They tell what's good (or bad) about packages used for specific brands or products, and what improvements should be made.

EDUCATION AND SUCCESS IN SELLING. By V. Harley Morgan. *University of Washington Business Review* (Bureau of Business Research, University of Washington, Seattle 5, Wash.), October, 1960. 75 cents. To determine the relationship between education and success in selling, the author conducted a study in which sales managers were asked to designate their "most successful," "average," and "least successful" industrial salesmen. The salesmen then

filled out questionnaires concerning their level of education, major in college, type of product sold, and kind of client contacted. Results indicated that a college education is an important determinant of success.

HOW TO IDENTIFY YOUR BEST BUSINESS CUSTOMERS. *Management Methods* (22 West Putnam Avenue, Greenwich, Conn.), November, 1960. Reprints 50 cents. Three kinds of companies compose this country's business market: (1) midgets—countless in number, they are small in size, costly to sell to, and buy only a small fraction of what is sold; (2) giants—a handful of large companies, they form a major, but not the biggest, portion of the market, and are not the easiest to sell to; and (3) "middle billions" firms—although middle-sized, they compose a multibillion-dollar segment of the market. For the first time, some newly uncovered facts about the middle-billions market are presented in this research analysis, which tells how to identify and sell to firms in this market.

PRODUCTION

UNDERSTANDING NUMERICAL POSITIONING CONTROL. By J. A. Baker. *Plant Engineering* (308 East James Street, Barrington, Ill.), October, 1960. \$1.00. Numerical positioning control—the use of simple numbers as machine instructions to produce a part automatically—is explained and illustrated in this article, which compares it, step by step, with the conventional method of making a part. Because the numerical method uses punched tape, it has many advantages, such as making design changes possible by simply changing the tape. Moreover, a jig is no longer needed to locate holes, nor does the operator need a detailed drawing; the

operator's only concern is to keep part blanks in the machine, since the control is responsible for producing the part.

HOW TO GET MORE FOR YOUR HIGH-STRENGTH STEELS DOLLARS. *Iron Age* (Chestnut and 56th Streets, Philadelphia 39, Pa.), October 6, 1960. Reprints gratis. Which family of high-strength steels is best for you? Is it the high-strength group with a yield strength of 50,000 psi? The superstrength steels? Or the ultrastrength steels? This article gives a rundown on each family, including examples, properties—which hinge on the alloy used—and applica-

Please order directly from publishers

tions. Generally, the high-strength steels are used if lowest cost per unit of strength or service is important; the superstrength steels provide more strength than the high-strength family; and the ultrastrong steels, while used now mostly for aircraft and missile parts, are beginning to be used in parts for other kinds of heavily stressed equipment.

MACHINE JOB LOTS ON PRODUCTION LINES. By A. O. Putnam. *American Machinist/Metalworking Manufacturing* (330 West 42 Street, New York 36, N.Y.), November 28, 1960. Reprints 25 cents. Because of the low-lot quantities in which many equipment manufacturers must make thousands of minor parts, set-up and idle time between operations is high, and large backlogs of work in process build up. To solve these problems, Jones and Lamson developed a technique to manufacture small-lot-size parts on a production-line operation—a technique they estimate will save

them \$300,000 a year. They will use a series of production lines, with each line assigned to parts which are similar; before making new layouts, however, they use a simulation technique—the Monte Carlo Game analysis—that makes it possible to predict end results under all conceivable conditions.

COMPRESSED AIR SYSTEMS. *Factory* (330 West 42 Street, New York 36, N.Y.), October, 1960. \$1.00. Specialists who were interviewed estimated that in eight out of ten plants where inadequacies exist in compressed air systems, the trouble is in the distribution system, not the compressor—and leakage is the greatest single cause of trouble. This article not only gives advantages of using compressed air, but also offers information designed to help evaluate plant air system performance, avoid common errors in system layout and operation, get the data needed to manage compressed air, and expand and modernize air systems most efficiently.

OFFICE

HOW TO BUILD A DATA PROCESSING DEPARTMENT. By Howard Ellis. *Modern Office Procedures* (812 Huron Road, Cleveland 15, Ohio), November, 1960. 75 cents. How can you tell when it's time to make the move to computers? How can you decide what equipment will do the job best? Data-processing experts at Du Pont recommend a gradual move from conventional tabulating equipment to punched-card and tape equipment, and finally to electronic data processing. There is no set formula, they say, that tells a company that their record-keeping equipment and procedures are overloaded—it takes constant checking to find if a change in procedure will save time and money. Guides to follow in selecting equipment are discussed, and the case histories of six firms that have installed electronic data-processing equipment are presented.

HOW TO SET UP AND OPERATE A RECORDS STORAGE CENTER. By J. F. Cummings and W. B. Sadauskas. *The Office* (232 Madison Avenue, New York, 16, N.Y.), December, 1960. Back issues \$1.00. To determine how active your records are, place a records-reference survey form at the front of any file drawer in question, and make an entry on the form every time one of the records is consulted. In time, the form will indicate which records are being used; those that are not should be moved to a permanent records center. The operation of such a center involves keeping track of the records, which are stored in cartons so that they can be checked out, if necessary. After installation, a records center containing about 3,000 cartons and having a moderate rate of record retrieval can be operated by one person.

Please order directly from publishers

Foreign Suppliers

(Continued from page 8)

There is little doubt that domestic sources can provide such added values as these more effectively and more consistently than foreign suppliers can.

The same check list includes many other useful and valuable services that can usually be better supplied by domestic than by foreign sources of supply. Under headings of "Availability," "Buying Convenience," and "Sales Assistance," these pertinent questions are raised:

- Does supplier have commitments to other customers which could affect my order?
- Does supplier have a local sales contact? Is he qualified to help me? Can he call upon specialists for my difficult problems?
- Will supplier help me cut acquisition costs such as qualifying visits, telephone calls, lab tests, incoming inspections, spoilage and waste, rejects and complaints?
- Will the supplier's reputation enhance acceptance of my product with his product as a component?
- Will the supplier provide selling aids?
- Does the supplier help develop mutual markets?

How much these added values are worth will, of course, depend on the individual purchaser and the individual supplier. The important point is that they should not be ignored merely because they are not reflected in price statistics.

OTHER ADVANTAGES

Many of the other differences between domestic and foreign suppliers are also qualitative and not easily reduced to price terms. For example, the relationship between the domestic supplier and the purchaser is likely to be more functional. The kind of company-to-company relationships that can develop when supplier and buyer operate as part of the same industrial community cannot develop when they are separated by oceans and by different national, political, and cultural traditions. Suppliers and purchasers within the same general geographic area are sensitive to one another's needs

"Domestic suppliers must compete not only in price, but also in terms of total value offered, including such added values as technical services, research, design assistance, and marketing aids . . ."

• • •

and to the fundamental functions of production, consumption, and merchandising; the foreign supplier necessarily is much more sensitive to world market price changes than he is to the special needs of a particular customer—in the United States or in any of his other export markets. The much closer character of the domestic supplier-purchaser relationship offers the opportunity for mutual understanding, out of which develop loyalties that can pay off in times of emergency or shortages.

Reliance on overseas suppliers also exposes the company to foreign political stresses and strains and adds another unknown to the already complicated and changing purchasing picture. To take an extreme example, consider the unenviable predicament of a company that depends on Cuba as a major source of supply for an essential material or component.

TYPES OF COMPETITION

In addition to these factors, domestic sources are in many ways more competitive than sources overseas. The very size of the United States economy means that normally there are more United States suppliers to choose from than there are in other countries, where suppliers are not only fewer in number, but have less of a competitive tradition. As exporters, foreign suppliers compete largely in terms of price; domestic suppliers must compete not only in price, but also in terms of total value offered, including such added values as technical services, research, design assistance, and marketing aids. These factors are so important that many purchasers prefer domestic sources of supply, even when they do not offer the greatest price-tag advantage.

Domestic sources offer the purchaser the benefits of competition between supplier *industries*, as well as the competition among supplier companies within an industry. This development is particularly evident among such key industrial materials as steel, copper, aluminum, glass, plastics, fibers (synthetic and natural), wood, and paper. Nowhere is this double competition among suppliers as advanced or as intense as it is in the United States.

FOREIGN IMPORTS

These factors have induced many corporations to stick with their domestic suppliers even when foreign sources could undersell them. But another consideration that has kept many companies in the domestic market is that foreign purchasing often cannot perform the desired end of keeping the company competitive with foreign imports. In fact, a shift to foreign supply sources frequently brings foreign competition in its wake. This occurs because the purchase of foreign raw materials and components automatically makes available in foreign countries information on the size and character of the United States market. Such data are especially useful to prospective foreign competitors in determining the cost-price spreads they will have to beat to undersell domestic companies.

In one industry after another, the same general pattern has developed: A U.S. manufacturing company buys a raw material or component at a price advantage overseas and before long finds itself being undersold in its own market by the finished product made in its entirety overseas. This unhappy experience has befallen companies making such diverse products as transistor radios, clothing, and aluminum cooking utensils, and the changing pattern of U.S. imports generally reflects this trend. More and more, the United States is importing finished products, not raw materials or components.

The importation of finished products has changed the character of many domestic markets. The American manufacturer is hard put to compete on the basis of price because of his inability to match the costs of foreign manufacturers, particularly the labor costs. To reduce his own costs, he may eliminate many of the added values mentioned earlier: the sales, research, market, and product-development services. Thus the activities that have made American industry

a leader in the development of new and improved products are starved out in this type of price competition.

But even when these steps have been taken, domestic manufacturers will usually find that they still cannot compete on a price basis with foreign firms. Overseas purchasing may narrow the advantages of foreign manufacturers with respect to the cost of materials or components, but it does not offset the other cost advantages enjoyed by foreign manufacturers. Thus the unavoidable and unpleasant conclusion is that foreign purchasing cannot be counted on to enable the domestic company to meet the competition of imports into United States markets.

FOREIGN OPERATIONS

Faced with this situation, more and more companies have been turning to foreign operations in their quest for price competitiveness. But the export drive of recent months has not produced the kind of penetration of foreign markets that can mean added sales for most manufacturing companies. Export gains have been largely confined to raw cotton and jet transport planes; in the area of manufactured goods generally, no significant change has occurred. Actually, exports account for a slightly *declining* share of the nation's total sales of manufactured products. Since 1955, we have been exporting about 4½ per cent of our manufactured goods. The export share went up to 4.76 per cent in 1957, retreated to 4.54 per cent in 1958, and amounted to 4.45 per cent for the first seven months of 1960. We are finding it difficult to expand our exports for exactly the same reason we find it difficult to compete against imports in our domestic markets: the wide gap between foreign and domestic manufacturing costs.

As a consequence, more and more companies are finding that in order to sell abroad they must manufacture abroad, to take advantage of the lower wage rates that prevail in other countries. This trend has been accelerated by the development of regional trade blocs, such as the European Common Market, which make it all the more necessary to get inside of external tariff walls in order to compete successfully.

Decisions to manufacture abroad have resulted in huge dollar commitments to foreign operations. In the field of manufacturing,

"We cannot take for granted that unrestrained international competition, under today's unbalanced world economic conditions, will bring us the net benefits that domestic competition has brought us to date . . ."

• • •

for example, exclusive of petroleum and metals mining, U.S. investments overseas have jumped from \$830 million in 1959 to an estimated \$1.2 billion in 1961—a 50 per cent jump in a two-year period.

Whether such activities prove to be right or wrong for the individual company, the net result has been to displace the output of United States plants and force the unemployment of those who would ordinarily be working in such plants. Even when foreign investments do not cause the closing of U.S. plants, as in industries where the rate of growth is great enough to accommodate all producers, they are at least foreclosing the future growth of capacity in those industries inside the United States and diverting the growth to foreign countries.

FREE TRADE?

World trade has played a much smaller part in building our economy than it has in other countries. The competition that has helped our economy to grow has been preponderantly domestic rather than international. We cannot take for granted that unrestrained international competition, under today's unbalanced world economic conditions, will bring us the net benefits that domestic competition has brought us to date.

It would be futile to rely on the lowering of barriers alone to develop our economy, ignoring the differences in the world's economies. The United States economy is on a plateau far above that of any other, and such a policy would be to the advantage of economies where prices and wages are lowest. A policy that encourages the purchase and manufacture of goods outside the United States will

eventually lead to a situation where individual companies will be losing more in United States markets than they can gain in cost savings through foreign operations or purchases. In other words, over any length of time, no company or industry can expect to buy supplies or to manufacture on the basis of low foreign wages and sell its products in the United States market on the basis of the traditionally higher wages paid here.

POLICIES FOR THE FUTURE

Needless to say, changes in the purchasing policies of U.S. companies will not be enough to solve this complex, many-sided problem. For the individual company, faced with the problem of reducing costs and remaining competitive, purchasing will necessarily be conducted on the basis of the particular situation in which the company finds itself, not on the basis of the balance of trade or the growth of the economy as a whole.

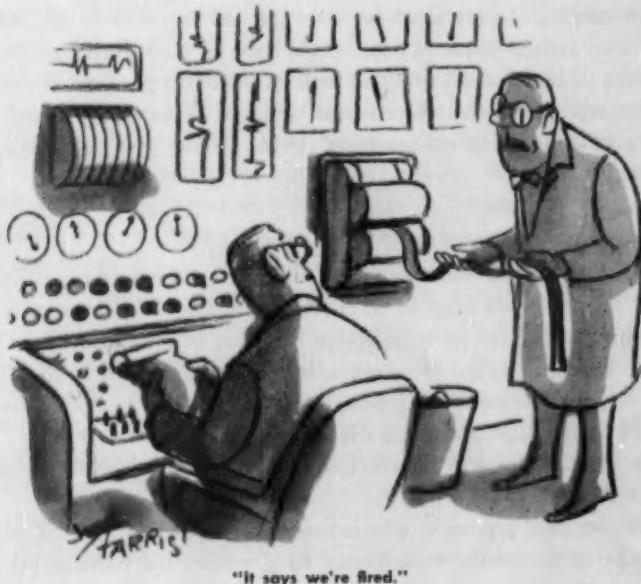
Nevertheless, it is time for every company to take a hard look at its own purchasing policies, to insure that it is not losing more in total value than it is gaining in price advantage by switching to foreign suppliers of materials and components. It would be short-sighted in the extreme to overlook the advantages of stability, familiarity with the market, technical capability, and buying convenience, as well as the sales, research, design, and marketing assistance that are offered by many domestic suppliers, if a lower price is all that is offered in exchange.

To solve the broader problems of the economy as a whole, guidelines are needed to help industry to establish policies that will develop a pattern of foreign trade—whether it be in terms of purchases, sales, or overseas operations—based on principles that will promote the growth of all markets, domestic and foreign. Such criteria would have to take account of the many political and economic considerations, governmental and industrial, that affect international trade. They would have to make allowance for the tremendous gaps between the economies of different nations and the necessity of narrowing these gaps before the forces of free trade can function properly—narrowing them by raising the levels of other economies rather than by lowering our own.

The solution cannot be worked out within the confines of govern-

mental bureaus, nor settled by industry alone. It is a problem that will require a tremendous amount of government-industry cooperation and effort, for it has many individual parts that must be fitted together if a sound answer for each company, for each industry, and for the nation is to be found.

The right kind of policy is no longer the haphazard sum of what each government official does at the government-to-government level and what each individual company does daily in the marketplace. In each of these areas, every effort is already being made to meet the day-to-day practical problems. But the continuing, longer-range problem of reconciling our economy with the economies of other nations cannot be solved this way. The right kind of policy—for purchasing, manufacturing, or selling—is one that, in conjunction with the policies of the government, other companies, and other industries, will help to promote and maintain economic health and growth, both here and abroad. ♦



Executive Compensation

(Continued from page 14)

The number of participants has a very real bearing on the size of the bonuses that can be granted to individuals—and, conversely, the size of bonus deemed desirable for different positions has a bearing on the number of executives who can participate in the plan.

In many companies, the bonuses paid are too small and extend too far down into the organization. Often, these companies have not thought out what they are trying to accomplish with incentive bonus plans and what they expect to gain through the payment of a bonus. It is hard to believe, for example, that improved corporate results are achieved by granting a \$7,500-a-year cost accountant or production scheduler a bonus of \$400 to \$500 on the basis of the profit-and-loss statement, yet payments of this size at this level are not uncommon.

In addition, in many plans there is a fairly common tendency to increase the number of participants each year. This usually reduces the amount of each individual's bonus, thus further weakening the incentive effect of the plan.

An effective bonus must be large enough to motivate the individual to secure future results. In a year of good corporate fiscal showing, a bonus opportunity of at least 40 to 60 per cent of salary at the top-management levels and at least 30 to 40 per cent of salary at the middle-management levels should provide sustained motivation.

Distribution of Bonus

There are three basic ways of distributing the incentive bonus fund among those eligible to participate. The first is to prorate the fund among the participants on the basis of their salaries. This is the easiest way, but it is not always desirable, since it gives the lazy, incompetent executive exactly the same bonus as the brilliant, hard-working, and successful executive at the same salary level. In some cases, however, distribution based on salary proration will prove most effective.

The second approach, which more clearly utilizes the incentive concept, is to distribute the bonus fund among the participants on

the basis of the job performance and actual accomplishments of each manager. This approach requires that the major items of accountability for each management position be determined and expressed in the most specific and meaningful terms possible. It is not enough to say that an executive's objective must be to "maintain satisfactory net profits in the chemical division"; the statement of accountability should be more precise—as, for example, "Maintain net profits before taxes of 24 per cent or better on capital employed in the chemical division." Of course, not all statements of position accountability will lend themselves to such objective statements. It is virtually impossible, for example, to establish highly objective criteria for the director of public relations, and many aspects of other line positions, as well as most aspects of staff positions, must be measured or assessed on a much more subjective basis.

Subjective Evaluations

Although the word "subjective" has acquired a negative connotation in some management circles, subjective determinations are not necessarily erroneous or unfair; in fact, they must be made every day by executives deciding many kinds of business problems. The reluctance of some executives to have bonus awards determined on a purely subjective basis stems from the recognition that personal bias, favoritism, or merely poor judgment on the part of the person making the determination may result in an unfair distribution of the incentive bonus fund. But this problem can be overcome, at least in part, if the amount of each individual bonus award is recommended, with substantiating written reasons, by each participant's immediate superior, and then reviewed at successively higher levels of management. In addition to discouraging bias or favoritism, such a procedure also encourages a strong desire on the part of each manager to obtain the specific results desired by his superior. The best results are secured when specific performance objectives are predetermined in discussions between the participant and his immediate superior, then reviewed at a higher management level. In this way, each individual participates in the determination of his own job objectives, and a higher degree of understanding and interest is secured.

A third possible means of distributing an incentive bonus fund

is to combine these two basic approaches. The bonus-fund distribution might well be on the basis of a formula that would set aside a specific percentage of the over-all fund for the corporate officer group, to be prorated on the basis of officer salaries. This would give recognition to the "team" concept at this level. The remainder of the over-all fund might then be distributed on the basis of an appraisal of the performance of individual members of lower-level management, who presumably would work somewhat more independently.

In multiplant or multidivision companies, the over-all fund might be prorated among the various operating divisions on the basis of their relative contributions to corporate net income or their performance against predetermined operating standards. The distribution within each division could be handled in one or more of the ways previously discussed.

Obviously, a wide variety of possible means of distributing the over-all incentive bonus fund exist. The determination of the best and most effective method for any given corporate situation requires an analysis of the full management-compensation program, corporate policies and objectives, and past management performance, and a consideration of the practices and problems of the industry of which the corporation is a part.

DEFERRED COMPENSATION

Essentially, there are only two basic ways of reducing the tax impact on income received by corporate officers and managers. One way is through capital gains, and the other is by deferring a portion of current income to a later date when the recipient's total taxable income will be lower.

Typically, incentive bonus awards are paid in cash each year. The award is thus ordinary income for tax purposes, and much of it must be paid out as taxes. The net result is usually much different if all or part of the bonus is deferred until the recipient's retirement.

Take the example of a 55-year-old executive with a wife and two children, a salary of \$34,000, and no other source of income. Assume that he has a typical range of tax deductions, including mortgage interest and real estate taxes, of \$4,600. His federal income taxes then would amount to \$8,090. But when this hypo-

thetical executive receives an incentive bonus award of \$10,000, his tax becomes \$12,930. In other words, he can keep only \$5,160 of the \$10,000 award.

But suppose that instead of paying the award currently in cash the employer paid it on a deferred basis after the executive's retirement (or termination of employment) in ten or more equal annual installments. To illustrate the tax mathematics involved, let us further assume that the executive also received a \$10,000 incentive bonus award for each of the next nine years, and that each of these awards was also deferred on the same basis.

Then, starting at age 65 (retirement date) the individual's income might look like this: \$10,000 a year deferred income, \$6,000 a year pension payment, and \$2,088 a year from Social Security, based on the present law—a total annual income of \$18,088 a year.

In this hypothetical case, the taxable gross income is \$16,000, since Social Security payments are tax-free. However, assume that the individual still has four personal exemptions (\$2,400), even though his two children are grown, because he and his wife are both 65, and that he has modest tax deductions of \$1,600. His taxable income then is \$12,000, and his tax would be \$2,720 a year.

So instead of keeping only about 50 per cent of the awards when paid in cash each year, the individual in this case would keep over 75 per cent, or about \$25,000 more, by deferring payment of incentive bonus awards until after retirement.

Advantages and Drawbacks

From the point of view of the individual, however, there is one possible drawback to this plan: Continuing inflation might wipe out all or most of the tax saving. This objection can be overcome by using the incentive bonus awards to buy common stock in the company and delivering stock (and accrued dividends) to the individual in 40 or more equal quarterly installments after retirement or termination of employment. In most cases, such deferred stock awards will at least protect the individual against the ravages of inflation, and there is also a possibility that corporate growth will result in a considerable appreciation of stock values.

Deferred contingent stock awards also are in the best long-term interests of the shareholders of the company, since this approach

tends to focus executive attention on both corporate growth (to increase the value of the deferred stock) and current profits (to get more stock through additional incentive bonus awards).

Of course, in order to avoid the tax doctrines of "constructive receipt" and "present economic benefits," an element of contingency must be involved in the payment of deferred cash or stock awards. To protect the interests of the corporation, the elements of contingency should serve a useful business purpose. To protect the interests of the individual, the elements of contingency should be controllable by him. Accordingly, such plans commonly provide that the executive agrees to serve the corporation for a specified number of years, agrees not to invest or participate in a competitive business activity, agrees to be available for consultation after termination of employment, etc.

Also, to avoid the doctrine of constructive receipt, the individual cannot have freedom of choice as to whether or not he will take a current award in cash or on a deferred basis. As a practical matter, this means that a definite program must be established which provides that all participants in the incentive bonus plan who meet certain criteria will receive a specified portion of any future incentive bonus awards on a deferred basis.

Deferred compensation is attractive primarily to the older and higher-paid executive. Ordinarily, executives under age 50 and at a salary level of less than about \$30,000 a year are far more interested in current income than in deferred income, in spite of the tax savings that are possible.

Individual Contracts

There is another basic approach to deferred compensation applicable to the older and highly paid executive: the deferred compensation contract between the individual and the employer. The typical deferred pay contract provides payments to the executive for ten years after termination of active employment—usually from 20 to 50 per cent of the salary he was receiving at the time the commitment was made.

For example, Copperweld Steel Company's contract with its president provided for an annual salary of \$50,000 for full-time services, and \$20,000 annually for serving in an advisory capacity after his

full-time employment ceased. In case he died before receiving 120 monthly payments for advisory services, the remaining payments would be made to his beneficiaries.

To withstand the doctrines of constructive receipt and present economic benefits, and to help protect against possible stockholder suits, contracts deferring executive compensation should provide for a period of satisfactory active employment before any deferred payments are made and should make payment of the deferred compensation contingent upon the employee's meeting such conditions as those previously outlined.

The individual contract deferring compensation is a selective device with a fairly limited application. It is of interest primarily to the older and highly paid top executive, relatively close to retirement, who will benefit by the deferral of part of current income to a time when the tax impact will be reduced. From the point of

CRITERIA FOR DEFERRED COMPENSATION

Ordinarily, deferred compensation is most attractive to older and higher-paid executives. Younger executives at lower salary levels usually prefer to receive bonus payments as current income. This suggests combining age and salary as criteria for determining eligibility to receive deferred awards. For example, a plan could provide deferred awards as follows:

<i>Executive's Age</i>	<i>Executive's Salary</i>	<i>Percentage of Bonus Award to Be Deferred</i>
50 or more	\$30,000 up	25 per cent
55 or more	\$40,000 up	50 per cent
60 or more	\$50,000 up	75 per cent

Such figures are, of course, illustrative only. The exact formula for any given corporate situation can only be determined after an analysis of the personal economic situations of the executives involved and a consideration of their personal desires.

view of the company, there are also definite advantages in specific cases—as, for example, when a company is not able to pay enough current income to attract an executive who is already highly paid by another company or who has accrued non-vested pension rights with his present employer. Under these circumstances, deferred pay may be the only method of compensating the executive for the risk and disturbance involved in changing jobs.

STOCK-OPTION PLANS

Today, over half the companies whose stock is traded on the New York Stock Exchange have adopted stock-option plans for their officers and key employees, although there is a wide divergence in the prevalence of such plans in different industries. In growth industries, such as drugs and electronics, the majority of companies use such plans; in industries such as banking, utilities, and insurance, they are rarely encountered.

A restricted stock-option plan is a plan that conforms to the requirements of Section 421 of the Internal Revenue Code of 1954 in regard to the option price, option term, length of time stock must be held, etc. The use of such plans has become increasingly popular, not only because they insure an executive's interest in the growth and profitability of the company, but because they offer substantial tax advantages to the individuals concerned.

Assume, for example, that an executive in the 50 per cent tax bracket is granted an option to purchase 2,500 shares of his company's stock at a price of \$95 a share. The stock is selling at \$100 a share at the time the option is granted, and the option is for a ten-year period.

At the end of six years, the stock is selling for \$155 a share, and the executive exercises part of his option and purchases 2,000 shares at \$95 a share, at a cost to him of \$190,000. Six months later the stock is still selling at \$155 a share, and the executive sells his 2,000 shares for \$310,000. Before taxes he is ahead approximately \$120,000.

If the gain of \$120,000 were treated as ordinary income for tax purposes, the executive would have a net profit of approximately \$36,000 on the deal. However, in the example cited above, the \$120,000 would be taxed at the maximum capital gains tax rate

of 25 per cent, and he would have a net profit of \$90,000—two and one-half times as much.

Of course, the individual does not have to exercise any part of the option if he does not wish to do so. Should the stock price drop or fail to rise enough to make the transaction attractive, the option need not be exercised and the executive has not had to risk any money.

Stockholder Reaction

In most cases, stock-option plans must be approved by the stockholders before being placed in effect, and this sometimes poses problems. Some stockholders feel that stock options only dilute their equity, and disregard the compensating advantages: An option requires no cash outlay by the corporation and, as the optionee benefits, so do the shareholders through appreciation of stock values. Of course, four keys to stockholder reaction will be the recent trend of the stock price, the profitability of the company, the number of shares requested for option purposes, and the option price at which the shares will be granted to members of management.

A review of 100 stock-option plans in companies listed on the New York Stock Exchange showed that the shares of stock available for option purposes, as a percentage of the total number of common shares outstanding, ranged from 0.95 per cent to 14.40 per cent, with a median of 4.7 per cent of the outstanding shares available for options.

In most cases, the option can qualify as a restricted stock option even when the option price is as low as 85 per cent of the fair market value of the stock at the time of the grant. Nevertheless, the typical plan established today sets the option price at 95 per cent, and more and more companies are tending to use 100 per cent of the current stock price as the option price. Obviously, the higher the option price, the more appealing it is to the stockholder group that must approve the plan.

Participants

A few companies, such as Monsanto Chemical, Grand Union, and the Mead Corporation, extend their stock-option plans to most, if not all, of their employees. The prevailing practice, however, is to provide a stock-purchase plan for lower-level employees, with the

stock-option plan reserved as a compensation and incentive device for officers and other members of management. An analysis of 50 plans selected at random showed that in the median company only 30 out of 5,900 employees (or 0.5 per cent) were eligible to receive options.

Of course, the size of the option granted the average optionee will also affect the number of employees who can participate in the plan. The typical current option amounts to approximately two-and-one-half times the annual salary of the optionee at the time of the option grant. To provide real incentive effect, options should amount to from two to five times annual salary, with the larger options going to the higher-level executives. It is wise, however, to set a limit on the maximum size of any one option grant, specifying, for example, that no more than 10 to 15 per cent of the total number of shares available for option purposes may be granted to any one individual.

When the plan is approved and options are first granted, a substantial proportion of the shares available for option should be held in reserve for use during the future life of the plan. It might be well to hold 25 to 30 per cent of the approved shares in order to be able to attract executives from other companies when the need arises, grant additional options to current top executives in future years, and grant options to younger executives who receive promotions to more responsible management positions.

Too many companies grant stock options to employees who cannot possibly affect the value of the company's stock. In one case, an option was given to the pilot of the company plane, and in another, to the captain of a company yacht. At these levels, the option is usually neither understood nor exercised. The tax advantages of a stock option mean far more at the higher-income levels, and it is at these levels that the stock option is a significant compensation and motivation device.

AN EFFECTIVE PROGRAM

A sound management-compensation program will attract, retain, and motivate the managers needed for the current profitable operation of the business and for its future growth.

A truly effective program can only be evolved after a careful analysis has been made of the short- and long-term business objec-

tives of the company, the kinds and amounts of compensation currently utilized, and the personal situations of the executives involved.

Many companies have found that growth and expansion, with the resulting organizational changes that such growth inevitably brings, makes it necessary to conduct a complete, periodic review to insure that the company has a fair, equitable, and effective management-compensation program. ♦



"I forgot to spray my head."

Organizational Loyalty

(Continued from page 24)

The ten primary factors included on the list are these:

- Having work that is interesting to me.
- Knowing that I am doing useful work and doing it well.
- Knowing that my income from my work will be as high as conditions permit.
- Working with congenial people.
- Knowing that I will win advancement if I deserve it.
- Knowing that I shall continue having my job as long as I do my part.
- Having a fair and understanding boss.
- Having work that challenges me.
- Knowing of developments that relate to my work or may affect my work performance.
- Knowing definitely what is expected of me in my work.

The extent to which management can help a man fulfill these motivational needs will greatly determine the degree of employee loyalty generated and attained in the company. The company that tries to meet them as fully as possible will be rewarded with the loyalty of its employees; the company that ignores them will in time find itself saddled with employees who will remain only until another job opportunity comes along.

Group Morale

Organization is not only a hierarchy of officialdom and a structure for authority levels, division of work, and production—it is also a social system. Social science research in industry has indicated the importance of group membership to individuals on the job. We find evidence of the informal organization everywhere in the company—among salesmen, secretaries, building guards, accountants, engineers, personnel officials, and machinists. The employee wants to "belong" to a work group, especially a work group that is friendly, enjoys a good record of achievement in the company, and can be a source of pride to him. A group of this kind has an energizing effect on the man; it stimulates him to do his best on behalf of the group and for the good of the company.

Like an individual employee, a group sets for itself certain objectives, standards, and values, and it, too, has a state of morale. A group with poor morale is marked by bickering, absenteeism, tardiness, strain, poor quality of performance, dissatisfaction, and lack of communication among its members. Where there is good morale in the group, it is often reflected in a spirit of cooperation and enthusiasm, higher output, and a low record of absenteeism. One finds in this group good coordination and communication, effectiveness in pitching in, mutual esteem, and congenial personal relations.

Among the factors that influence the state of morale of the group—and hence the loyalty of its members to the company—these are the most important:

- The group's belief in top-management officials—its confidence in management.
- Its perception of management's goals, approaches, and methods as not too much in conflict with the group's goals and performance.
- The ease or difficulty in getting a good job done in the company.
- Opportunity for the group to participate in problem-solving and some decision-making in the organization.
- Absence of threat to the existence or stability of the group.
- Satisfactory work conditions and security for its members as employees.
- The opportunity to make a positive contribution, gain recognition, and derive a sense of accomplishment.
- Adequate communication-mindedness in the company.
- Its satisfaction with the competency of the supervisors as technicians and leaders.
- The group's degree of satisfaction with the extent to which the work is challenging and provides status to the job holders and opportunities for the members to learn and advance.

To the extent that management can provide these influences, it will build groups with esprit de corps, zeal, unity of objectives, and a bond of loyalty to the company. A company that is disdainful of the group and ignores these factors will contain, not cohesive groups

of workers, but merely bunches of men—and will find the loyalty potential greatly diminished.

BUILDING ORGANIZATIONAL LOYALTY

The task of attaining organization-centered loyalty requires responsiveness to the motivations of the individual employee and the morale of the work groups in the company—the two pillars of organizational loyalty. Just as there are many aspects of loyalty, the problem of building, reinforcing, and sustaining loyalty must be approached in various ways.

Communications

Management has to make clear what it is trying to do, why it is doing it, and how it expects to get it done. The communication effort must also make known the results of effort and tell people where they stand and how they're doing. Management should put out communication antennae to determine whether the requirements of individual motivation are being fulfilled and whether the morale of the work groups is at a high level.

Personnel Policies

Personnel policies that are well-conceived, clearly expressed in writing, and applied consistently and equitably will do much to engender employee loyalty. This is especially important in the case of policies governing a grievance system for non-unionized workers, merit rating, job evaluation, salary administration, fringe benefits, and training for more challenging assignments and possible advancement. A man wants to know just what he is asked to give his loyalty to, and the company creed and personnel policies provide him with many of the answers.

Supervision

Good supervision is crucial, for it can make or break the company in its effort to build employee loyalty. Informed judgment must be exercised in the selection of supervisors, adequate human relations training must be offered, and rigorous appraisal of supervisory capacity and performance in dealing with the individual employees and the work groups must be conducted.

"Honest difference of opinions or views is healthy in an organization, but undercurrents of conflict are divisive and impair the loyalty potential in the company . . ."

• • •

The company must insist on standards of supervisory performance that demand technical competency, firmness, fair-mindedness, and ability to stimulate employee motivation and group morale. It is a mistake to wait for complaints or grievances to erupt before doing anything about them; effective supervision can deal with problems early, before they become seriously disruptive to the working atmosphere. Such measures as attitude surveys can often help the supervisor to detect trouble while it is smoldering beneath the surface.

Dealing with Conflict

Where evidences of dissatisfaction show up, they should be handled promptly, since they will usually become worse as they remain dormant and unresolved. Management has to smoke out the causes of conflict within the ranks, bring them to the surface, and deal with them constructively by focusing on the issues and their implications rather than on personalities and emotions. Honest difference of opinions or views is healthy in an organization, but undercurrents of conflict are divisive and impair the loyalty potential in the company.

A common kind of conflict is found in men who have divided allegiance—conflict, for example, between the employee's allegiance to the company and to the union, between the foreman's allegiance to management and to his workers, or between the specialist's allegiance to his professional goals and to the best interests of the organization. To be sure, such dual allegiances are not always incompatible, but in many cases the opposing loyalties create indecision and stress for the individual concerned.

By clarifying the kind of loyalty it expects of such members of the organization, management can often help to resolve the conflict and help them to develop a clear sense of dual allegiance. In most cases, this is entirely possible and quite satisfactory from the company's point of view—but there will be occasions when each man will have to face up to certain issues that require him to cast his allegiance one way or the other. At this point, he must make his own decision, but he must realize that, if the issue is particularly vital and he does not choose the organization-centered value, he is necessarily placing his position in jeopardy.

MAN AND THE COMPANY

In brief, the individual employee wants to be treated with dignity, he wants to have his talents utilized in jobs that make demands on his abilities, initiative, and energy, he looks to fair play in both praise and blame, he expects to be told how he's doing, he believes there should be recognition of good work or performance, and he feels that he should be informed in advance of changes or developments that may affect his work setting or his performance. He looks to a reward system that includes nonfinancial as well as financial forms of recognition. He hopes there can be a reasonable reconciliation of the three sets of values—individual, group, and company. He believes that loyalty is a two-way affair, and he will give evidence of loyalty when management shows genuine interest in his problems and those of his work group.

A company can obtain organizational loyalty only by harnessing the many aspects of which it is composed. Broad appeals or demands can accomplish nothing if the fundamentals of motivation and morale have been overlooked. Fostering an atmosphere conducive to employee loyalty is a continuing, painstaking job that affects all areas of the organization. It isn't a simple task, but it is one that must be accomplished if the company is to move toward the realization of its organizational goals through the use of its human resources. ♦

EXPERIENCE is not what happens to a man. It is what a man does with what happens to him.

—Aldous Huxley



SURVEY OF BOOKS FOR EXECUTIVES

Contributions, Company Style

COMPANY GIVING. By Leo J. Shapiro. Survey Press, 814 North Michigan Avenue, Chicago, 1960. 136 pages with tables. \$4.75.

*Reviewed by Richard Eells**

The variety of recipients of company philanthropy is growing. Mr. Shapiro's explanation for this growth is succinct: "Until around 1930, almost all private donations went for direct relief—food, clothing, and shelter. Since that time, however, about 99 per cent of this direct relief has come to be handled by government agencies. This has freed the personal and company donations for use by private agencies, almost all of which are engaged in experimentation, prevention, eradication, pioneer-

ing, and counseling in specific areas." Today, the question is no longer whether to give, but *how* to give—and *how much*.

Mr. Shapiro's investigation of company giving in the five-county Chicago metropolitan area was sponsored by the Chicago Chapter of the Public Relations Society of America. He studied data (for 1956) from 513 companies and conducted interviews at 70 per cent of them. The companies were divided into six groups according to the number of personnel; in general, however, the findings are discussed in terms of small, medium, and large companies.

The study revealed that larger organizations support a greater variety of philanthropies than smaller ones do, but that middle-sized companies (500-1,000 employees) currently contribute the highest percentage of their net profit. Smaller companies tend to support causes that have direct or immediate appeal, such as religion or health. They also show a tendency toward defensive rather than purposeful giving. Larger companies

* Public Policy Consultant, General Electric Company.

favor such causes as education and youth groups. They give more to civic and public service groups, less to religious and sectarian organizations. As the text puts it: ". . . as company size increases, there is a tendency for company giving to reflect the corporation and not the individual, for giving to be an expression of corporate policy and not of personal whim."

The list of types of contribution is interesting. Although money is the usual contribution, many companies—notably the larger ones—also donate the time of their personnel. They lend men to help raise funds, or encourage them to volunteer for community service. Contributing merchandise is more popular in smaller companies.

An investigation of methods of giving showed that many companies have no formula, and that yearly contributions are often based on previous contributions, though they are sometimes based on profits or sales volume.

There is apparently no inclination to discontinue company contributions

or to question the need for them, even though public awareness of the contributions appears to be low. Only the largest companies get any considerable public credit for their philanthropies; the public seems to feel that such companies are prosperous, growing, and well-intentioned.

A text accompanies and clarifies the tables at the end of the book. Appendices describe the sampling, the procedure, the tables, and the questionnaire schedules, and include a copy of the questionnaire as well. There is, finally, an extensive bibliography on company giving.

Mr. Shapiro and his associates have done a conscientious and thorough job. They have produced a workman-like report whose principal conclusion seems to be that the major lack in company giving is a well-thought-out program. At present, written statements of contribution policy are not common, but Mr. Shapiro feels that their use will spread as company philanthropy becomes a part of long-range company programs.

Briefer Book Notes

(Please order books directly from publishers)

GENERAL

YOUR HEART: A Handbook for Laymen. By H. M. Marvin, M.D. Doubleday & Company, Inc., 501 Franklin Avenue, Garden City, N.Y., 1960. 335 pages. \$4.50. The author, a past president of the American Heart Association, describes the nature, symptoms, and effects of the more common heart diseases and disturbances, and the kinds of treatment now available. He also discusses the possibility of preventing heart disease and advises on the problems and rehabilitation of heart patients.

PRACTICAL HANDBOOK OF INDUSTRIAL TRAFFIC MANAGEMENT. (Third Edition.) By Richard C. Colton and Edmund S. Ward. The Traffic Service Corporation, 815 Washington Building, Washington 5, D.C., 1959. 411 pages. \$7.50. A complete revision of a widely used handbook. In addition to its comprehensive coverage of transportation problems, it deals with related fields like warehousing and packaging. Included are a glossary, a bibliography, and reprints of standard contracts.

INTERCOLLEGIATE BIBLIOGRAPHY: Cases in Business Administration. (Vol. IV.) Compiled by Virginia Jenness and Grace V. Lindfors. Intercollegiate Case Clearing House, Soldiers Field, Boston 63, Mass., 1959. 186 pages. Gratu. This 1959 edition lists 710 cases developed for use at 63 educational institutions and available through the Intercollegiate Case Clearing House. Classified by functional areas, the listing includes an abstract of each case and identification of its setting and the people involved. A listing of foreign language cases is also provided, together with a bibliography of motion pictures suitable for group discussion by management personnel.

A PRIMER FOR PROFIT IN THE STOCK MARKET: A Manual for the Small Investor. By Harry Kahn, Jr. Doubleday & Company, Inc., Garden City, New York, 1959. 239 pages. \$3.95. Intended for the prospective investor with little or no previous experience in the stock market, this guide suggests some basic principles he should follow. It also points out the pitfalls that often confront the beginner and explains how to use the various kinds of information available to investors. In the second half of the book, the author discusses the investment outlook for various industries.

THE QUALITY AND ECONOMIC SIGNIFICANCE OF ANTICIPATIONS DATA: A Conference of the Universities-National Bureau Committee for Economic Research. Princeton University Press, Princeton, N. J., 1960. 466 pages. \$9.00. The record of a conference held at Princeton in 1957 on the role of expectations in the decisions of government, industry, and individuals. Includes papers on the predictive value of anticipations data as an aid in forecasting and as evidence of how the economic process generates expectations.

HOW TO OBTAIN AND USE BUSINESS INFORMATION. By Vira de Sherbinin. Know Publications, Inc., 799 Broadway, New York 3, 1960. 67 pages. \$15.00. This practical guide to the use and planning of research in both large and small companies of all kinds includes advice on how to locate good sources of information, how to organize and administer the research department, and how to handle research materials. Lists of domestic and foreign sources and a basic bibliography are also provided.

COMMUNICATIONS IN BUSINESS AND INDUSTRY. By William M. Schutte and Erwin R. Steinberg. Holt, Rinehart and Winston, Inc., 383 Madison Avenue, New York 17, 1960. 393 pages. \$4.75. In addition to a systematic exposition of the basic principles of communication and its common problems, this text covers such specific applications as writing reports, writing to persuade, and communicating in group discussion. Illustrative material taken from a wide range of sources is appended to each chapter.

Publications Received

(Please order directly from publishers)

DIGITAL COMPUTER PRINCIPLES. By Wayne C. Irwin. D. Van Nostrand Company, Inc., 120 Alexander Street, Princeton, N. J., 1960. 321 pages. \$8.00.

CORPORATE RECORDS RETENTION: A Guide to Requirements of State Governments of the U.S. Prepared by Robert B. Wheelan. Controllers Institute Research Foundation, Inc., 2 Park Avenue, New York, 1960. 1,022 pages. \$20.00.

INTRODUCTION TO LINEAR PROGRAMMING. By R. Stansbury Stockton. Allyn and Bacon, Inc., 150 Tremont Street, Boston, Mass., 1960. 104 pages. \$2.25.

BIBLIOGRAPHY OF INTERNAL AUDITING: Supplement No. 1, Jan. 1, 1956 to Dec. 31, 1959. The Institute of Internal Auditors, 120 Wall Street, New York, 1960. 36 pages. \$1.50.

COMPARATIVE PUBLIC ADMINISTRATION: A Selective Annotated Bibliography (Second Edition). By Ferrel Heady and Sybil L. Stokes. Institute of Public Administration, The University of Michigan, Ann Arbor, Mich., 1960. 98 pages. \$3.00.

EQUITY CAPITAL AND SMALL BUSINESS. Small Business Administration, Washington, D. C., 1960. 78 pages. 35 cents.

HOW TO MAKE A HABIT OF SUCCESS. By Bernard Haldane. Prentice-Hall, Inc., 70 Fifth Avenue, New York 11, N.Y., 1960. 216 pages. \$4.95.

CREATIVE ENGINEERING DESIGN. By Harold R. Buhl. Iowa State University Press, Press Building, Ames, Iowa, 1960. 195 pages. \$3.95.

MODERN MANAGEMENT OF ENTERPRISES. By Henry K. Junckerstorff. Published by Martinus Nijhoff, 9 Lange Voorhout, P.O.B. 269, The Hague (Netherlands), 1960. 82 pages. 5.70 guilders (\$1.52).

EUROPEAN GUIDE TO GENERAL COURSES IN BUSINESS MANAGEMENT. Organization for European Economic Cooperation, 2, rue André Pascal, Paris XVI^e, France, 1960. 640 pages. \$4.50.

EXHAUSTION OF UNEMPLOYMENT BENEFITS DURING A RECESSION. By William Stanley Devino. Michigan State University, East Lansing, Mich., 1960. 70 pages. \$1.50.

REAL ESTATE INVESTMENT TRUSTS: New Income Tax Treatment. Commerce Clearing House, Inc., 4025 West Peterson Avenue, Chicago 46, Ill. 31 pages. \$1.00.

CURRENT SOURCES OF MARKETING INFORMATION. Edited by Edgar Gunther. American Marketing Association, 27 East Monroe Street, Chicago 3, Ill., 1960. 119 pages. Members, \$2.00; nonmembers, \$4.00.

LEGAL REASONING: The Evolutionary Process of Law. By William Zelemyer. Prentice-Hall, Inc. 70 Fifth Avenue, New York 11, N.Y., 1960. 174 pages. \$4.35.

BIBLIOGRAPHY ON PLANNING. Edited by Blair E. Olmstead. Published by The College on Planning of the Institute of Management Sciences. The Prudential Insurance Co. of America, Prudential Plaza, Newark 1, N. J., 1960. 16 pages. TIMS members \$1.25; nonmembers, \$2.00.

*A history of management thought—
by those who made the history . . .*

CLASSICS IN MANAGEMENT

SELECTIONS FROM THE
HISTORIC LITERATURE OF MANAGEMENT

Until now, many of the classics of management have been hidden in private collections or scattered in reference libraries. As a result, these timeless ideas have been largely unavailable to managers and other students of management.

Yet, these pioneering concepts are the foundation of modern management practice. They express the principles that have made management a profession and have molded business and industry in the western world.

Every executive should be familiar with this heritage. He can be—through CLASSICS IN MANAGEMENT. This one book offers an absorbing picture of the development of management theory and practice. Each selection was chosen for its inherent interest and enduring value.

CLASSICS IN MANAGEMENT belongs on the shelf of every manager who believes that he is a professional worker in a field with a history, a heritage, and a future.

Critical introduction, notes, bibliography
Clothbinding, 446 pages
\$9.00/AMA members: \$6.00

American Management Association, Inc.

Q&A on AMA



Q. Our company has recently established an office that will serve as a central source of information on the management development and training meetings sponsored by the various local, regional, and national organizations. How can this office stay up to date on future AMA meetings in all subject areas?

A. The Association will furnish an individual or office having this responsibility with detailed announcements of all forthcoming AMA sessions. A request for this service, which is provided without charge, should be forwarded to the Member Relations Department at AMA headquarters. Be sure to specify the address to be used for this material.

* If you have any questions about AMA's program or policies, please submit them to AMA's Member Relations Department. All inquiries will be answered promptly. Those questions of most general interest will appear in this feature in subsequent issues of *The Management Review*.

